

IN THE
Supreme Court of the United States

OCTOBER TERM, A. D. 1943.

No.

WISCONSIN GAS & ELECTRIC COMPANY,
Petitioner,

vs.

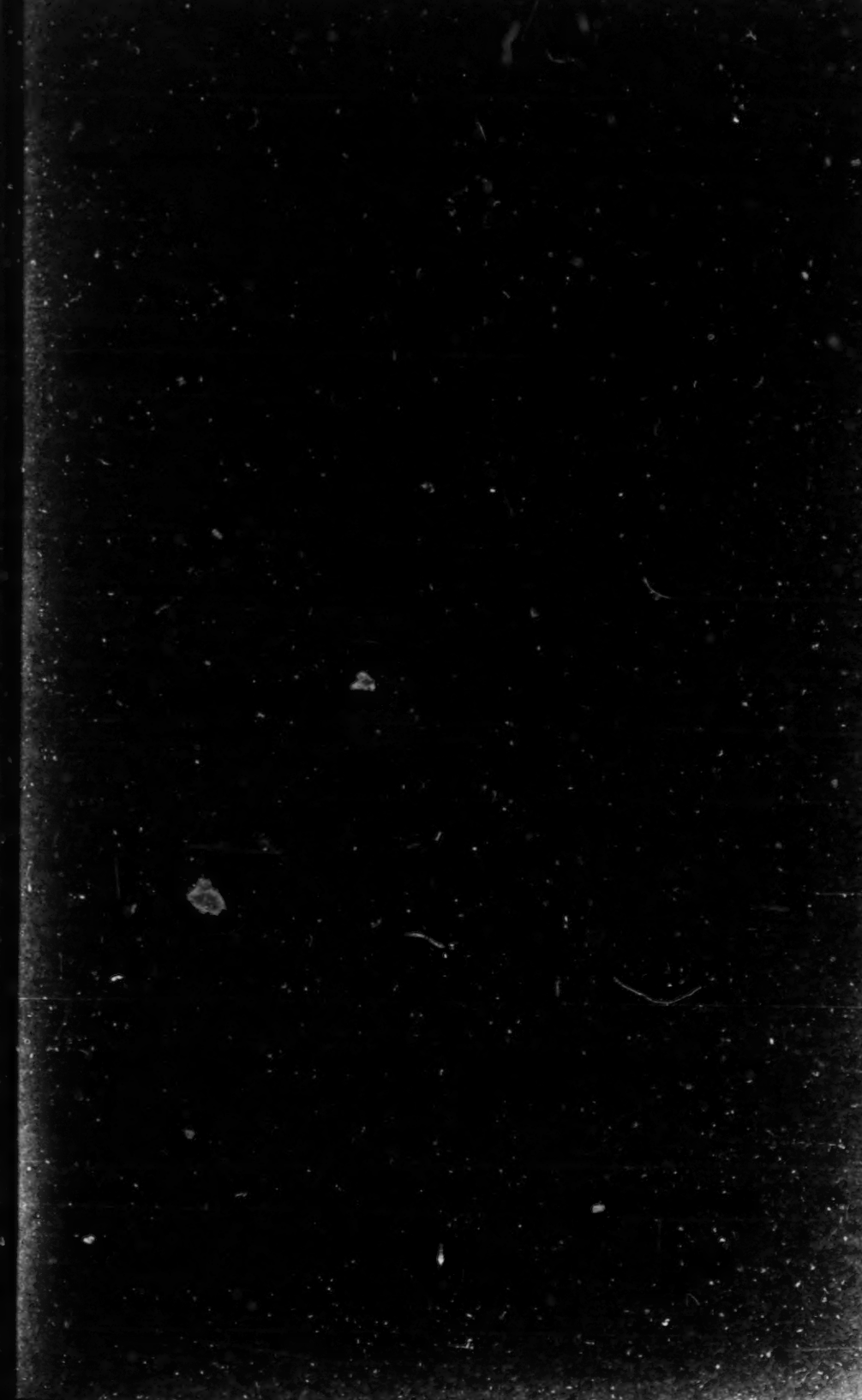
THE UNITED STATES OF AMERICA,
Respondent.

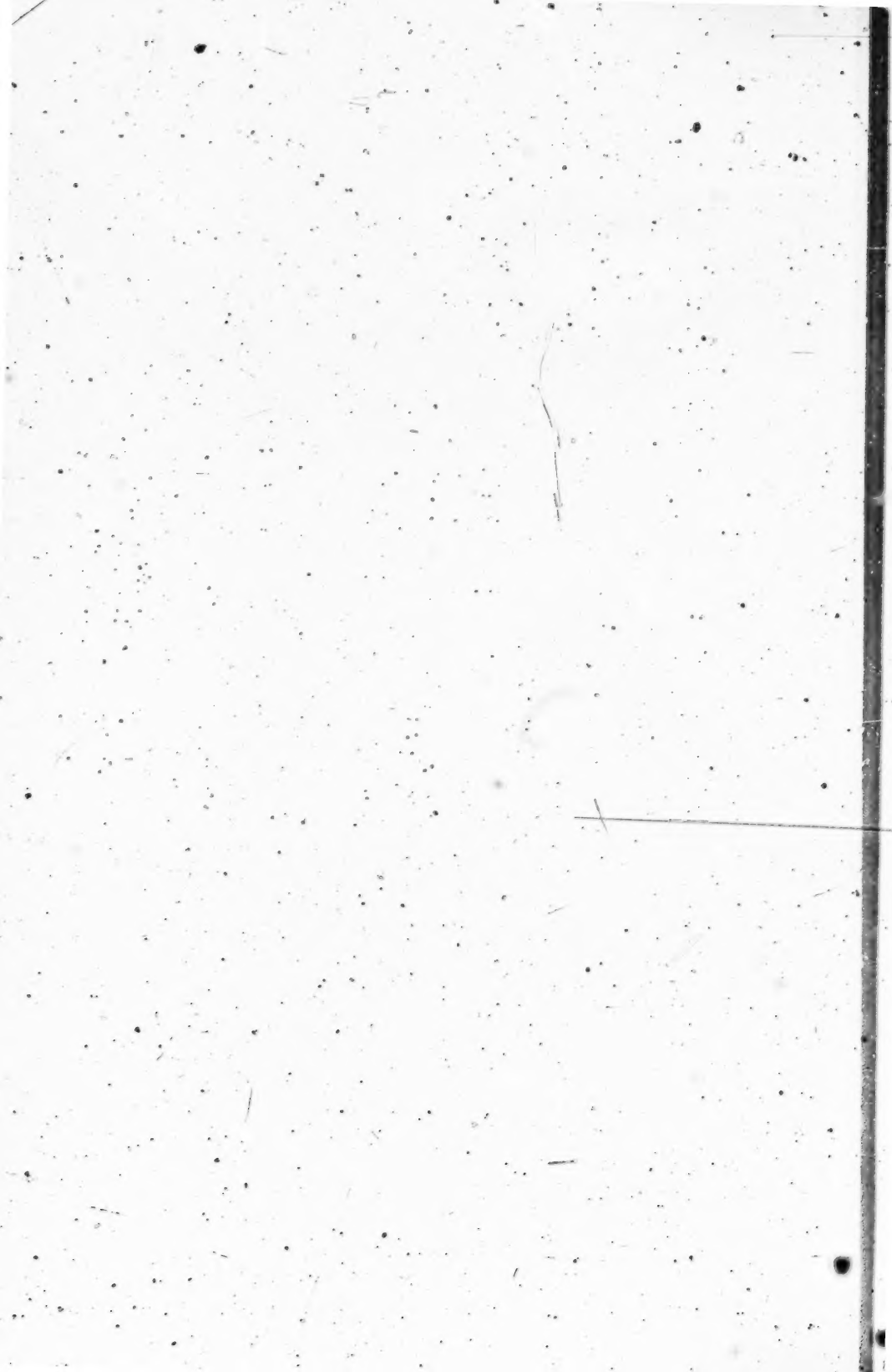
ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF
APPEALS FOR THE SEVENTH CIRCUIT.



INDEX.

| | |
|---|----|
| Index to printed record of proceedings in U. S. District Court | i |
| Clerk's certificate to printed record of proceedings in U. S. District Court: | 15 |
| Index to Proceedings in U. S. Court of Appeals: | |
| Placita | 17 |
| Appearance for Appellee, filed March 26, 1943.... | 17 |
| Appearance for Appellant, filed April 27, 1943... | 18 |
| Order taking cause under advisement, entered Oct. 12, 1943 | 19 |
| Opinion by Minton, C. J., filed November 8, 1943.. | 20 |
| Judgment, entered November 8, 1943..... | 23 |
| Clerk's Certificate | 25 |
| Order allowing certiorari | 26 |





**In the
United States Circuit Court of Appeals
For the Seventh Circuit**

No. 8276

WISCONSIN GAS & ELECTRIC COMPANY,
Plaintiff-Appellee,

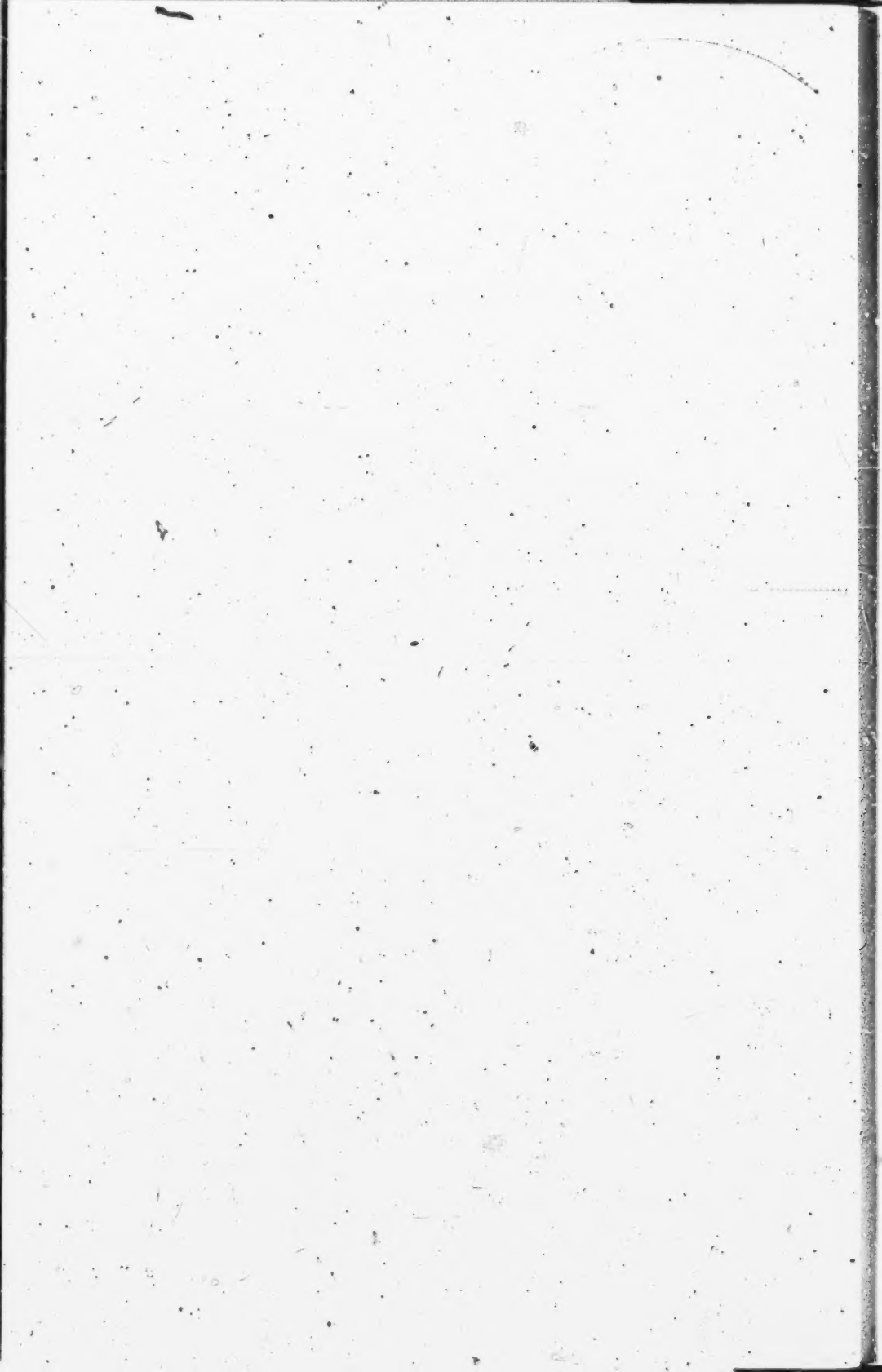
vs.

THE UNITED STATES OF AMERICA,
Defendant-Appellant.

**Appeal from the District Court of the United States for
the Eastern District of Wisconsin.**

INDEX

| | |
|---|----|
| Placita | 1 |
| Complaint, filed Feb. 19, 1941..... | 2 |
| Answer, filed Apr. 15, 1941..... | 4 |
| Stipulation of Facts filed Apr. 22, 1942..... | 5 |
| Opinion, filed Sept. 25, 1942..... | 6 |
| Findings of Fact, etc., filed Oct. 5, 1942..... | 9 |
| Judgment, entered Oct. 6, 1942..... | 10 |
| Notice of Appeal, filed Dec. 29, 1942..... | 11 |
| Assignment of Errors..... | 12 |
| Order extending time to file transcript of record.... | 13 |
| Designation of Record..... | 13 |
| Clerk's Certificate..... | 14 |



DISTRICT COURT OF THE UNITED STATES

Placita.

For the Eastern District of Wisconsin.

United States of America, } ss:
Eastern District of Wisconsin.

At a stated term of the District Court of the United States of America, for the Eastern District of Wisconsin, begun and held at the City of Milwaukee, in said District, on the first Monday (being the 5th day) of October, A. D. 1942;

Present, the Honorable F. Ryan Duffy, Judge of said Court, presiding;

Among other the following proceedings were had, to-wit:

| | |
|--|----------------------------|
| Wisconsin Gas & Electric Com- pany, | } Civil Action No. 468. |
| <i>Plaintiff,</i> | |
| <i>vs.</i> | |
| United States of America, | |
| <i>Defendant.</i> | |

Be it remembered that heretofore, to-wit: on the 19th day of February, A. D. 1941, came the plaintiff and filed its complaint against the defendant as follows:

Filed
Feb. 19,
1941.

3 IN THE DISTRICT COURT OF THE UNITED STATES.
• • (Caption—468) • •

To the Honorable Judge of the District Court for the Eastern District of Wisconsin:

Plaintiff, Wisconsin Gas & Electric Company, for a complaint herein against the defendant alleges and shows to the court:

1. Plaintiff Wisconsin Gas & Electric Company is a corporation duly organized and existing under the laws of the State of Wisconsin and is and has been engaged for a period of more than twenty years, pursuant to its articles of incorporation, in the conduct of an electric utility and other public service businesses wholly within the State of Wisconsin; that the plaintiff is and was at all times mentioned herein a resident and citizen of the eastern district of Wisconsin.

2. This is a suit of a civil nature brought to recover internal revenue taxes known as income taxes unlawfully imposed upon and collected by the defendant from the plaintiff and now held and retained by the defendant.

3. The amount in controversy, exclusive of interest and costs, is the sum of Five hundred fifteen and 63/100 (\$515.63) dollars. The suit arises under the laws of the United States relating to the recovery of refundable

4 excess internal revenue taxes, and jurisdiction is conferred upon this court by paragraph 20 of Section 24 of the Judicial Code (U. S. C. A., Title 28, Section 41-(20)).

4. Plaintiff's federal income taxes for the year 1935 were assessed and collected on the basis of the disallowance to the plaintiff of Wisconsin Dividend Privilege Taxes accruing and paid by it in the year 1935 in the amount of Three thousand seven hundred fifty (\$3,750.00) dollars. By reason of the disallowance of such payment, the income taxes assessed to and paid by the plaintiff for the year 1935 were Five hundred fifteen and 63/100 (\$515.63) dollars in excess of the amount of such taxes justly due and owing. The last payment made by the plaintiff on account of such taxes was made May 10th, 1937, and exceeded the said amount of Five hundred fifteen and 63/100 (\$515.63) dollars.

5. On May 9th, 1939, claim for refund in said amount was duly filed with the Collector of Internal Revenue at

Complaint.

3

Milwaukee, and thereafter on October 31st, 1940, the Commissioner of Internal Revenue rejected and disallowed such claim for refund. The true nature of the Wisconsin Dividend Privilege Tax has now been adjudicated by the United States Supreme Court from which adjudication it appears that payments on account of such taxes are deductible in ascertaining the amount of the corporate taxpayer's income for federal income tax purposes.

Wherefore, plaintiff demands judgment against the defendant pursuant to law in the said sum of Five hundred fifteen and 63/100 (\$515.63) dollars, with interest from December 15th, 1936, as provided by law.

/s/ James D. Shaw,
Attorney for Plaintiff Wisconsin Gas & Electric Company.

5 State of Wisconsin. }
Milwaukee County. } ss.

L. F. Seybold, being first duly sworn, on oath says: that he has read the foregoing complaint, knows the contents thereof and is informed and believes that the same is true; that this verification is made by affiant for the reason that the plaintiff is a corporation and he is an officer thereof, to wit, Vice President, and is duly authorized to make this verification for and on its behalf.

L. F. SEYBOLD.

Subscribed and sworn to before me this 13th day of February, 1941.

(Seal)

Robert B. Fisher,
Notary Public, Milwaukee
County, Wisconsin.

My commission expires November 26, 1944.

Endorsed: "Filed Feb. 19, 1941. B. H. Westfahl,
Clerk."

Filed
Apr. 15,
1941.

IN THE DISTRICT COURT OF THE UNITED STATES.

* * (Caption—468) * *

ANSWER.

Defendant, by its attorney, Berthold J. Husting, United States Attorney for the Eastern District of Wisconsin, answering the complaint in this action:

I.

Admits the allegations contained in Paragraphs "1", and "3" of the complaint.

II.

Denies the allegations of Paragraph "2" of the complaint, except that it admits that the action brought by the plaintiff is of a civil nature for the recovery of internal revenue taxes known as income taxes.

III.

Admits the allegations of Paragraph "4", except that it denies the second sentence in said paragraph.

IV.

Admits the allegations of Paragraph "5" of the complaint, except that it denies the last sentence of said paragraph.

Wherefore, defendant prays for judgment against the plaintiff, dismissing the complaint, together with the costs and disbursements of this action.

B. J. Husting,
Berthold J. Husting,
United States Attorney,
Attorney for the Defendant.

By E. J. Koelzer,
Assistant,
358 Federal Bldg.,
Milwaukee, Wis.

Endorsed: "Filed Apr. 15, 1941. B. H. Westfahl, Clerk."

7 IN THE DISTRICT COURT OF THE UNITED STATES.
 • • (Caption—468) • •

Filed
 Apr. 22,
 1942.

STIPULATION FOR AGREED STATEMENT OF FACTS.

The parties hereto by their respective attorneys hereby agree that the issues in the above entitled action may be submitted for decision on the briefs of the parties and upon the following Agreed Statement of Facts:

1. Plaintiff, Wisconsin Gas & Electric Company, is and was during the tax year in question a Wisconsin corporation engaged, pursuant to its articles of incorporation, solely in an electric utility, gas utility, street railway or trackless trolley and steam heating business and in the sale of electric and gas appliances in connection with its said electric and gas utility businesses. All of such businesses were conducted wholly within the State of Wisconsin.

2. In a tentative return for the year 1935, filed by plaintiff on March 13, 1936, an estimated tax liability of \$43,312 was disclosed. Thereafter, on June 12, 1936, a completed corporation income and excess-profits return based on the accrual method for the calendar year 1935 showing a total tax liability of \$42,212.13 was filed.

3. Taxes in the amount of \$715,538.15 were claimed as deductions under Item 19 of the return. A schedule 8 attached to the return contained a complete analysis of the claimed deductions and disclosed that Privilege Dividend Tax amounting to \$3,750 paid to the State of Wisconsin was taken as a deduction.

4. The said privilege dividend taxes of \$3,750 paid to the State of Wisconsin for 1935 resulted from the declaration and payment of dividends by plaintiff during said year out of earnings from its public utility businesses. The said taxes were computed in accordance with Laws of Wisconsin, 1935, c. 505, as amended by Laws of Wisconsin, 1935, c. 552.

5. As a result of an examination of the books and records of the taxpayer by an Internal Revenue Agent, an additional tax in the amount of \$11,696.00 with interest thereon in the amount of \$847.96, totaling \$12,543.96, was

assessed. In addition to the disallowance of certain items not challenged by the plaintiff, the agent disallowed as a deduction the Wisconsin Privilege Dividend Tax of \$3,750.

The amount of \$12,504.30 was paid by the taxpayer on May 10, 1937, and on October 26, 1937, the remainder of the assessment, namely \$39.26, was abated.

6. On May 9, 1939, the taxpayer timely filed with the Collector of Internal Revenue for the District of Wisconsin, a claim for refund on two grounds, one of which relates to the issue herein.

On October 31, 1940, the taxpayer was officially notified of the rejection of the claim for refund in respect to the claimed deduction for dividend taxes paid to the State of Wisconsin.

7. This controversy involving \$515.65 in income taxes for the year 1935, arises solely from the disallowance of plaintiff's claim for deduction of the amount of Wisconsin privilege dividend taxes paid for the tax year 1935.

James D. Shaw,
Van B. Wake,

Attorneys for Plaintiff.

April 17th, 1942.

B. J. Husting,
*United States Attorney for the
Eastern District of Wisconsin.*

By E. J. Koelzer,
Asst. U. S. Atty.

Endorsed: "Filed Apr. 22, 1942. B. H. Westfahl,
Clerk."

Filed
Sept. 25,
1942.

9 IN THE DISTRICT COURT OF THE UNITED STATES.

• • (Caption—468) • •

OPINION.

Plaintiff is a Wisconsin corporation. During the year 1935, as a result of declaration of dividends during that year, plaintiff paid to the State of Wisconsin the sum of \$3,750.00 as privilege dividend taxes. In computing its federal income tax for that year, plaintiff sought to claim such payment as a deduction allowed under Sec. 23(c) of the Revenue Act of 1934, but the claim was disallowed. A

claim for refund was timely made and was rejected by the Commissioner.

The Wisconsin privilege dividend tax is imposed by Sec. 3 of Chapter 505, Laws of Wisconsin for 1935, as amended. The tax is computed at a percentage of the dividends declared and paid out of corporate earnings derived from property located and business transacted in Wisconsin. The act states the tax is imposed "for the privilege of declaring and receiving dividends, out of income derived from property located and business
10 transacted in this state."

Sec. 23, Revenue Act of 1934, C. 277, 48 Stat. 680, provided:

"Sec. 23. Deductions from Gross Income.

"In computing net income there shall be allowed as deductions:

"(c)" Taxes Generally. Taxes paid or accrued within the taxable year, except"

(The exceptions have no application here.)

The question to be decided is whether the plaintiff corporation is entitled to a deduction from its gross income for the year 1935 for the amount of the privilege dividend tax paid to the State of Wisconsin during the taxable year. The government contends that the tax was imposed on the shareholders of the corporation for dividends received, and that the corporation was merely a withholding or collecting agent. While admitting that the statute made the corporation liable for the collection of the tax, the government contends that this was only to insure and simplify tax collections.

The validity of the Wisconsin privilege dividend tax was challenged and the Wisconsin Supreme Court in *J. C. Penney Co. v. Tax Commission*, 233 Wis. 286, held that the tax was an excise tax and invalid in respect to foreign corporations exercising the dividend privileges outside of the State of Wisconsin, notwithstanding the transaction of business, the earning of income, and the presence of stockholders
11 within the State of Wisconsin. On appeal to the

United States Supreme Court, the Wisconsin court was reversed. *Wisconsin et al. v. J. C. Penney Co.*, 311 U. S. 435. The court divided, five to four, the majority opinion being written by Justice Frankfurter. The contention made by the government here that the tax was on the stock-

holders received support in the dissenting opinion by Justice Roberts, who said (p. 448):

"* * * By the very terms of the Act, the tax is laid not on the corporation but on the stockholder receiving the dividend and, by confession, thousands of such stockholders are not residents of Wisconsin. The corporation is the mere collector of the tax and the penalty for failure to collect it is that the corporation must pay it. If the exaction is an income tax in any sense it is such upon the stockholder and is obviously bad. It cannot, except by a perversion of the term and the affixing of an arbitrary label, be denominated a tax upon the income of the respondent."

We would be strongly inclined to agree with the opinion expressed by the minority, but are bound to follow the conclusion of the majority opinion, which states (p. 442):

"* * * The practical operation of this legislation is to impose an additional tax on corporate earnings within Wisconsin but to postpone the liability for this tax until such earnings are paid out in dividends. In a word, by its general income tax Wisconsin taxes corporate income that is taken in; by the Privilege Dividend Tax of 1935 Wisconsin superimposed upon this income tax a tax on corporate income that is paid out."

These words of the majority opinion cannot be lightly brushed aside. On this point there was a direct and emphatic conflict with the viewpoint of the minority. If the

Wisconsin privilege dividend Tax "is to impose an additional tax on corporate earnings," and if "by the

Privilege Dividend Tax of 1935 Wisconsin superimposed upon this income tax a tax on corporate income that is paid out," then there can be little doubt but that the majority of the Supreme Court held the tax to be on the corporation and not upon the shareholders. It is apparent that the validity of the tax was upheld on that basis.

This court is bound by the United States Supreme Court decision in the *Penney* case, *supra*, and it therefore follows that judgment must go for the plaintiff.

Dated at Milwaukee, Wisconsin, this 25th day of September, A. D. 1942.

F. Ryan Duffy,
Judge.

Endorsed: "Filed Sept. 25, 1942. B. H. Westfahl, Clerk."

13 IN THE UNITED STATES DISTRICT COURT.

* * (Caption—468) * *

Filed
Oct. 5,
1942.

FINDINGS OF FACT AND CONCLUSIONS OF LAW.

1. This action is brought pursuant to Subdivision (20) of Section 24 of the Judicial Code within the time limited by law for the recovery of internal revenue tax in a sum less than Ten thousand (\$10,000.00) dollars alleged to have been erroneously or illegally assessed or collected.

2. Plaintiff, a Wisconsin corporation, at all times material hereto had its principal office and place of business in the Eastern District of Wisconsin and within the jurisdiction of this Court. That at all times material hereto plaintiff was engaged pursuant to its Articles of Incorporation solely in an electric utility, gas utility, street railway and trackless trolley and steam heating businesses and in the sale of electric and gas appliances in connection with its electric and gas utility businesses. All of such businesses were conducted wholly within the State of Wisconsin.

3. Plaintiff in this action filed on February 19th, 1941, seeks the refund of \$515.63, representing part of the corporate income taxes paid by it for the year 1935.

4. The claimed excess of \$515.63 in income taxes for the year 1935 resulted from the disallowance by an internal revenue agent of \$3,750.00 taken as a deduction by the plaintiff and representing dividend privilege taxes in 14 said sum of \$3,750.00 paid by the plaintiff to the State of Wisconsin for the year 1935 and during the year 1935 in consequence of the declaration and payment by the plaintiff during said year out of earnings from its public utility businesses. Such dividend privilege taxes were computed in accordance with the Laws of the State of Wisconsin for 1935, Chapter 505, as amended by the Laws of 1935, Chapter 552.

5. The last payment made by the plaintiff on account of corporate income taxes for the year 1935 was on May 10, 1937, and exceeded said amount of \$515.63.

6. On May 9, 1935, the taxpayer timely filed with the Collector of Internal Revenue for the Eastern District of Wisconsin a claim for refund, including the amount sought in this action. On October 31, 1940, the Commissioner of

Internal Revenue rejected and disallowed such claim for refund.

Upon the foregoing findings of fact the Court makes and enters the following conclusions of law:

Conclusions of Law.

1. Pursuant to the provisions of Section 23, Revenue Act of 1934, 48 Stat. 680, plaintiff is entitled to the deduction from its gross income for the year 1935 of the amount of privilege dividend tax paid to the State of Wisconsin during the taxable year.

2. Privilege dividend tax so paid is not within the exceptions to deductible taxes as set forth in said Section 23 of the Revenue Act of 1934.

3. Plaintiff is entitled to recover the sum of \$515.63 with interest at 6% per annum from December 15, 1936.

15 The Clerk of this Court is hereby directed to enter judgment accordingly.

Dated, at Milwaukee, Wisconsin, this 5th day of October, 1942.

F. Ryan Duffy,
Judge.

Endorsed: "Filed Oct. 5, 1942. B. H. Westfahl, Clerk."

Entered
Oct. 6,
1942.

16 And afterwards, to-wit: on the second day of said Term, to-wit: on the 6th day of October, A. D. 1942, the following proceedings were had, to-wit:

IN THE UNITED STATES DISTRICT COURT.
• • (Caption—468) • •

JUDGMENT.

The Court having filed its findings of fact and conclusions of law herein directing the entry of judgment in favor of the plaintiff and against the defendant; it is

Adjudged, that the plaintiff, Wisconsin Gas & Electric Company, do have and recover of the defendant, The United States of America, the sum of Five hundred fifteen

Notice of Appeal.

11

and 63/100 (\$515.63) dollars with interest thereon according to law from December 15, 1936.

Dated, October 6th, 1942.

By the Court,

B. H. Westphal,
Clerk.

Endorsed: "Filed Oct. 6, 1942. B. H. Westfahl, Clerk."

19 IN THE DISTRICT COURT OF THE UNITED STATES
OF AMERICA

Filed
Dec. 29,
1942.

For the Eastern District of Wisconsin.

| | |
|-----------------------------------|----------------------------|
| Wisconsin Gas & Electric Company, | } Civil Action No. 468. |
| <i>Plaintiff,</i> | |
| <i>vs.</i> | |
| The United States of America, | |
| <i>Defendant.</i> | |

NOTICE OF APPEAL.

Notice is hereby given that the United States of America, the defendant above-named, hereby appeals to the Circuit Court of Appeals for the Seventh Circuit from the judgment entered in this action on the 6th day of October, 1942, in favor of the plaintiff and from the whole thereof.

B. J. Husting,

*United States Attorney for the
Eastern District of Wisconsin.*

By E. J. Koelzer,

*Assistant United States Attorney
for the Eastern District of
Wisconsin.*

*Attorney for appellant, United
States of America.*

*Rm. 358, Federal Building,
Milwaukee, Wisconsin.*

Endorsed: "Filed Dec. 29, 1942. B. H. Westfahl, Clerk."

Filed
Mar. 19,
1943.

17 IN THE UNITED STATES CIRCUIT COURT OF APPEALS.

For the Seventh Circuit.

| | |
|-----------------------------------|----------------------------|
| United States of America, | } Civil Action No. 468. |
| <i>Appellant,</i> | |
| <i>vs.</i> | |
| Wisconsin Gas & Electric Company, | } <i>Appellee.</i> |
| | |

ASSIGNMENT OF ERRORS.

Now comes the United States of America, appellant in the above-entitled cause, and files the following assignment of errors upon which it will rely in the prosecution of this appeal in the above-named case from the judgment of the District Court of the United States for the Eastern District of Wisconsin, entered on October 6, 1942.

1.

The District Court erred in its finding that the privilege dividend taxes involved, in the sum of \$3,750.00, were paid by appellee to the State of Wisconsin, to the extent that said finding suggests that the payment of privilege dividend tax referred to was made by appellee as principal rather than as agent for either its stockholders or the State of Wisconsin.

2.

The District Court erred in its conclusion that pursuant to the provisions of Sec. 23, Revenue Act of 1934, 48 Stat. 680, appellee is entitled to the deduction from its gross income for the year 1935 of the amount of privilege dividend tax paid to the State of Wisconsin during the taxable year.

18 The District Court erred in its conclusion that appellee is entitled to recover the sum of \$515.63 with interest at 6% per annum from December 15, 1936.

Wherefore appellant prays that said judgment may be

reversed and that such other and further relief may be granted as to this Court may seem just and proper.

B. J. Husting,
United States Attorney.

Endorsed: "Filed Mar. 19, 1943. B. H. Westfahl,
Clerk."

20 IN THE DISTRICT COURT OF THE UNITED STATES.

• • (Caption—468) • •

Entered
Jan. 18,
1943.

**ORDER EXTENDING TIME FOR FILING RECORD
ON APPEAL AND DOCKETING ACTION.**

The above-named defendant, United States of America, having on December 29, 1942, filed its notice on appeal from the judgment entered in this action on the 6th day of October, 1942, upon application of said defendant and appellant;

It Is Ordered that the time for filing the record on appeal and docketing the action be and it hereby is extended to ninety days from December 29, 1942.

Dated at Milwaukee, Wisconsin, this 18th day of January, 1943.

F. Ryan Duffy,
United States District Judge.

Endorsed: "Filed Jan. 18, 1943. B. H. Westfahl,
Clerk."

21 IN THE UNITED STATES DISTRICT COURT.

• • (Caption—468) • •

Filed
Mar. 12,
1943

DESIGNATION OF RECORD ON APPEAL

Appellant, defendant in above entitled action, designates the following portions of the record, proceedings and evidence to be contained in the record on appeal in the above entitled case:

1. The Complaint.
2. The Answer.
3. The Stipulation of Facts.

Clerk's Certificate.

4. Opinion of Court directing judgment in favor of Plaintiff.
5. Findings of Fact and Conclusions of Law.
6. Judgment in favor of Plaintiff.
7. Notice of Appeal, with date of filing.
8. Order filed January 18, 1943, extending time for filing Record on Appeal.
9. Assignment of Errors.
10. This Designation.

B. J. Husting,
*United States Attorney, Eastern
 District of Wisconsin,*
 By: Elsmere J. Koelzer,
*Assistant United States
 Attorney,*
 358 Federal Building,
 Milwaukee, Wisconsin.

Endorsed: "Filed Mar. 19, 1943. B. H. Westfahl,
 Clerk."

22

CERTIFICATE OF CLERK.

United States of America, }
 Eastern District of Wisconsin. } ss.

I, B. H. Westfahl, Clerk of the District Court of the United States of America for the Eastern District of Wisconsin, do hereby certify that I have compared the writings annexed to this certificate, which are copies, with their originals now on file and remaining of record in my office, and that they are true copies of the pleadings, judgment and other papers; in the case of Wisconsin Gas & Electric Company vs. United States of America, No. 468 Civil Action.

In Testimony Whereof, I have hereunto set my hand and duly affixed the seal of said Court at the City of Milwaukee, in said district, this 25th day of March, in the year of our Lord, one thousand nine hundred forty-three, and of the Independence of the United States, the 167th.

(Seal)

B. H. Westfahl,
 Clerk.

UNITED STATES CIRCUIT COURT OF APPEALS.

For the Seventh Circuit.

I, Kenneth J. Carrick, Clerk of the United States Circuit Court of Appeals for the Seventh Circuit, do hereby certify that the foregoing printed pages contain a true copy of the printed record, printed under my supervision and filed on the twenty-second day of April, 1943, in:

Cause No. 8276.

Wisconsin Gas & Electric Company,
Plaintiff-Appellee,

vs.

The United States of America,
Defendant-Appellant.

as the same remains upon the files and records of the United States Circuit Court of Appeals for the Seventh Circuit.

In Testimony Whereof I hereunto subscribe my name and affix the seal of said United States Circuit Court of Appeals for the Seventh Circuit, at the City of Chicago; this 14th day of December, A. D. 1943.

(Seal)

(signed) Kenneth J. Carrick,
*Clerk of the United States Circuit Court
of Appeals for the Seventh Circuit.*

[illegible]

At a regular term of the United States Circuit Court of Appeals for the Seventh Circuit, held in the City of Chicago, and begun on the sixth day of October, in the year of our Lord one thousand nine hundred and forty-two, and of our Independence, the one hundred and sixty-seventh.

Wisconsin Gas & Electric Company,
Plaintiff-Appellee,

8276

vs.

The United States of America,
Defendant-Appellant.

} Appeal from the District
Court of the United
States for the Eastern
District of Wisconsin.

And, to-wit: On the twenty-sixth day of March, 1943, there was filed in the office of the Clerk of this Court, an appearance of counsel for appellee, which said appearance is in the words and figures following, to-wit:

IN THE UNITED STATES CIRCUIT COURT OF APPEALS,

For the Seventh Circuit.

Wisconsin Gas & Electric Company,
Plaintiff-Appellee,

vs.

The United States of America,
Defendant-Appellant.

} No. 8276.

The Clerk will enter our appearance as counsel for the plaintiff and appellee, Wisconsin Gas & Electric Company.

Dated, February 4th, 1943.

James D. Shaw,
Van B. Wake.

P. O. Address:

773 North Broadway,
Milwaukee, Wisconsin.

Endorsed: Filed March 26, 1943. Kenneth J. Carrick,
Clerk.

Appearance for Appellant.

And afterwards, to-wit: On the twenty-seventh day of April, 1943, there was filed in the office of the Clerk of this Court, an appearance of counsel for appellant, which said appearance is in the words and figures following, to-wit:

UNITED STATES CIRCUIT COURT OF APPEALS,

For the Seventh Circuit.

Cause No. 8276.

United States of America,

Appellant,

vs.

Wisconsin Gas & Electric Company,

Appellee.

The Clerk will enter our appearance as counsel for Appellant.

Samuel O. Clark, Jr.,
Assistant Attorney General,
Department of Justice,
Washington, D. C.

Sewall Key,
Special Assistant to the At-
torney General,
Department of Justice,
Washington, D. C.

Indorsed: Filed April 27, 1943. Kenneth J. Carrick,
Clerk.

And afterwards, to-wit: On the twelfth day of October, 1943, the following further proceedings were had and entered of record, to-wit:

Tuesday, October 12, 1943.

Court met pursuant to adjournment.

Before:

Hon. J. Earl Major, Circuit Judge.
Hon. Sherman Minton, Circuit Judge.
Hon. Walter Lindley, District Judge.

Wisconsin Gas & Electric Company,

Plaintiff-Appellee,

8276

vs.

The United States of America,

Defendant-Appellant.

} Appeal from the District
Court of the United
States for the Eastern
District of Wisconsin.

Now this day come the parties by their counsel, and this cause comes on to be heard on the transcript of the record and the briefs of counsel, and on oral argument by Mr. Fred E. Youngman, counsel for appellant, and by Mr. James D. Shaw, counsel for appellee, and the Court takes this matter under advisement.

And afterwards, to-wit: On the eighth day of November, 1943, there was filed in the office of the Clerk of this Court, the Opinion of the Court, which said Opinion is in the words and figures following, to-wit:

IN THE UNITED STATES CIRCUIT COURT OF APPEALS,
For the Seventh Circuit.

No. 8276.

October Term and Session, 1943.

WISCONSIN GAS & ELECTRIC COM-
PANY,

vs. *Plaintiff-Appellee,*

THE UNITED STATES OF AMERICA,
Defendant-Appellant.

Appeal from the District
Court of the United
States for the Eastern
District of Wisconsin.

November 8, 1943.

Before MAJOR and MINTON, *Circuit Judges*, and LINDLEY,
District Judge.

MINTON, *Circuit Judge.* The State of Wisconsin has what is called the Privilege Dividend Tax Law. The pertinent provisions thereof we set forth in the margin.¹

1. "SECTION 3. PRIVILEGE DIVIDEND TAX. (1) For the privilege of declaring and receiving dividends, out of income derived from property located and business transacted in this state, there is hereby imposed a tax equal to two and one-half per centum of the amount of such dividends declared and paid by all corporations (foreign and local), except those specified in paragraphs (d) and (g) of subsection (1) of Section 71.05 of the statutes, after the passage and publication of this act and prior to July 1, 1937. Such tax shall be deducted and withheld from such dividends payable to residents and non-residents by the payor corporation.

"(2) Every corporation required to deduct and withhold any tax under this section shall, on or before the last day of the month following the payment of the dividend, make returns thereof and pay the tax to the tax commission, reporting such tax on the forms to be prescribed by the tax commission.

"(3) Every such corporation hereby made liable for such tax, shall deduct the amount of such tax from the dividends so declared.

"(4) In the case of corporations doing business within and without the state of Wisconsin, such tax shall apply only to dividends declared and paid out of income derived from business transacted and prop-

The Wisconsin Gas and Electric Company, the plaintiff-appellee, is a utility corporation whose total business is done in Wisconsin. It is a Wisconsin corporation. In 1935 the plaintiff declared a dividend of \$150,000. It distributed \$146,250 to its stockholders, and paid 2½% of the dividend declared, or \$3,750, to the Tax Department of the State of Wisconsin. The plaintiff deducted this \$3,750 as an expense on its Federal income tax return for 1935. The Commissioner disallowed the deduction and assessed a deficiency. The plaintiff paid the assessment and sued to recover what it claimed to be an excessive assessment. The District Court sustained the position of the plaintiff, and gave judgment accordingly. From this judgment, the Government has appealed.

The sole question is whether the plaintiff was entitled to deduct in 1935 under Sec. 23(c) of the Revenue Act of 1934 the amounts paid pursuant to the Wisconsin Privilege Dividend Tax Law. The answer to this question depends upon whose burden it is to pay this tax.

The power of Wisconsin to exact such a tax was upheld by the United States Supreme Court in *Wisconsin v. J. C. Penney Co.*, 311 U. S. 435, 61 S. Ct. 246, 85 L. Ed. 267. Since that decision, the Supreme Court of Wisconsin has answered the question as to where this burden rests. In the case of *Wisconsin Gas & Electric Company v. Wisconsin Tax Department*, 243 Wis. 216, 10 N. W. (2d) 140, the Wisconsin Gas and Electric Company, the same company that is the plaintiff here, claimed the payment of the Privilege Dividend Tax as a deductible expense against its gross income under the Income Tax Law of Wisconsin, just as it is claiming here the payment of such tax as a deductible expense under the Federal statute. The Supreme Court of Wisconsin denied such claim, saying:

"We are certain of three things: (1) that the burden of the tax is specifically laid upon the stockholder;

erty located within the state of Wisconsin. The amount of income attributable to this state shall be computed in accordance with the provisions of chapter 71. In the absence of proof to the contrary, such dividends shall be presumed to have been paid out of earnings of such corporation attributable to Wisconsin under the provisions of chapter 71, for the year immediately preceding the payment of such dividend. If a corporation had a loss for the year prior to the payment of the dividend, the tax commission, shall, upon application, determine the portion of such dividend paid out of corporate surplus and undivided profits derived from business transacted and property located within the state."

(2) that the corporation declaring the dividend must deduct the tax from the dividend and may not under any circumstances treat the tax as a necessary expense of doing business; (3) that the power to levy the tax so construed was authoritatively established in the *Peñney* case."

On the same day, the Supreme Court of Wisconsin decided *Blid v. Wisconsin Foundry and Machine Co.*, 243 Wis. 221, 10 N. W. (2d) 142. In that case, a preferred stockholder sued the defendant corporation to recover from it the amount it had withheld from a dividend it had declared, and which amount the corporation had paid over to the State of Wisconsin in literal compliance with Sec. 3, Chap. 505 of the Wisconsin Laws of 1935, as amended. The plaintiff's contention was that while the language seems to place the tax on the stockholder, it must be ignored in view of the fact that the corporation alone is liable for the tax and the penalties if not paid, and there is no personal liability imposed on the stockholder. A demurrer to the complaint was sustained, the complaint dismissed, and from this judgment an appeal to the Wisconsin Supreme Court was taken. On the authority of *Wisconsin Gas & Electric Company v. Wisconsin Tax Department*, *supra*, the cause was affirmed.

Thus it will be seen that the Supreme Court of Wisconsin has decided very clearly that the burden of this tax is upon the stockholder and not upon the corporation, and that it was not an expense of the corporation.

In determining who is liable for a State tax and who may deduct it as an expense, the Federal courts will follow the decisions of the State courts. *Keith v. Johnson*, 271 U. S. 1, 8, 46 S. Ct. 415, 70 L. Ed. 795; *Magruder v. Supplee*, 316 U. S. 394, 396, 62 S. Ct. 1162, 86 L. Ed. 1525.

In the case at bar, the tax is laid against the dividend. If there is no dividend declared, there is no tax. When a dividend is declared, it is the property of the stockholder, and he may sue for it as a debt due him from the corporation. *Chesapeake and Delaware Canal Co. v. United States*, 250 U. S. 123, 126, 39 S. Ct. 407, 63 L. Ed. 889.

At the time this case was decided by the District Court, the Supreme Court of Wisconsin had not decided *Wisconsin Gas & Electric Company v. Wisconsin Tax Department*, *supra*, and *Bied v. Wisconsin Foundry and Machine*

Company, supra. The trial court relied upon *Wisconsin v. J. C. Penney Co.*, 311 U. S. 435, 61 S. Ct. 246, 85 L. Ed. 267. The reasoning of that case would seem to sustain the District Court's position. Power to tax was the only question before the court in the *Penney* case. Who shall be entitled to enjoy some incidence of the tax payment is our question. In view of the facts that the plaintiff is a Wisconsin corporation and all of its business is done in Wisconsin, and that there is no finding that any of its stockholders are non-residents of Wisconsin, the factual situation is clearly distinguishable from the *Penney* case.

We think the plaintiff was not entitled to claim the deduction, and that the deficiency was correctly determined. The judgment of the District Court is

REVERSED.

Endorsed: Filed November 8, 1943. Kenneth J. Carrick, Clerk.

And on the same day, to-wit: On the eighth day of November, 1943, the following further proceedings were had and entered of record, to-wit:

Wisconsin Gas & Electric Company,

Plaintiff-Appellee;

8276

vs.

The United States of America,

Defendant-Appellant;

} Appeal from the District
Court of the United
States for the Eastern
District of Wisconsin.

This cause came on to be heard on the transcript of the record from the District Court of the United States for the Eastern District of Wisconsin, and was argued by counsel.

On consideration whereof, it is ordered and adjudged by this Court that the judgment of the said District Court in this cause appealed from be, and the same is hereby, reversed, and that this cause be, and the same is hereby, remanded to the said District Court.

8

UNITED STATES CIRCUIT COURT OF APPEALS.

For the Seventh Circuit.

I, Kenneth J. Carrick, Clerk of the United States Circuit Court of Appeals for the Seventh Circuit, do hereby certify that the foregoing printed pages contain a true copy of the proceedings had and papers filed, excepting briefs of counsel and motions and orders extending time for filing briefs, in:

Cause No. 8276.

Wisconsin Gas & Electric Company,
Plaintiff-Appellee,

vs.

The United States of America,
Defendant-Appellant,

as the same remains upon the files and records of the United States Circuit Court of Appeals for the Seventh Circuit.

In Testimony Whereof I hereunto subscribe my name and affix the seal of said United States Circuit Court of Appeals for the Seventh Circuit, at the City of Chicago, this 14th day of December, A. D. 1943.

(signed) Kenneth J. Carrick,
*Clerk of the United States Circuit Court
of Appeals for the Seventh Circuit.*

(Seal)



SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed January 31, 1944

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Seventh Circuit is granted, and the case is transferred to the summary docket.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

(421)

Doc. No. 100-100000
FILED
SEP 22 1941
FEDERAL BUREAU OF INVESTIGATION
U. S. DEPARTMENT OF JUSTICE

TO THE HONORABLE SENATOR
FRANK J. LAURENCE
WASHINGTON, D. C.

FROM THE
WESTERN ELECTRIC COMPANY
Pittsburgh, Pa.

UNITED STATES OF AMERICA

Dear Senator: I am pleased to see the United States
Senate has taken an interest in the General Electric
and Westinghouse Trust.

Yours truly,
JAMES W. WAKE,
Attorney for the Trust,
272 North Broadway,
Milwaukee (2), Wisconsin.

INDEX.

| | Page |
|--|------|
| Petition: | |
| Caption | 1 |
| Opinions Below | 2 |
| Jurisdiction | 2 |
| Summary Statement | 2 |
| Statutes Involved | 3 |
| Questions Presented | 3 |
| Reasons for Granting the Writ | 4 |
| Brief: | |
| Opinions Below | 7 |
| Jurisdiction | 7 |
| Summary Statement | 7 |
| Specification of Errors | 9 |
| Summary of Argument | 9 |
| Argument: | |
| I. <i>The decision of the Circuit Court of Appeals decided a Federal question in a way probably in conflict with applicable decisions of this court</i> | 11 |
| II. <i>The decision of the Circuit Court of Appeals involves an important question of Federal law which should receive ultimate determination</i> | 17 |
| III. <i>The decision of the Circuit Court of Appeals involves, but leaves unanswered, the alternative contention of the applicability of Section 23 (d) of the Revenue Act of 1934. Such proposition would appear to raise an important question of Federal law not previously before this court but worthy of final disposition</i> | 19 |
| Conclusion | 21 |

Index—Continued.

| Appendix: | Page |
|--|------|
| Wisconsin Privilege Dividend Tax | 23 |
| Extract from the Revenue Act of 1934..... | 25 |
| Section 71.03(4) of the Wisconsin Statutes dealing with Wisconsin Income Taxes | 26 |
| Administrative Practice Concerning Wisconsin Privilege Dividend Tax | 26 |

AUTHORITIES.

Cases Cited:

| | |
|---|---------------|
| Biddle vs. Commissioner, 86 Fed. (2d) 718..... | 15 |
| Biddle vs. Commissioner of Internal Revenue, 302 U. S. 573 | 7, 15, 18, 20 |
| Blid vs. Wisconsin Foundry & Machine Co., 243 Wis. 221 | 14 |
| State ex rel. Froedtert Grain & Malting Co. vs. Tax Commission, 221 Wis. 225..... | 17 |
| International Harvester Co. vs. Department of Taxation, 243 Wis. 198-205 | 12 |
| International Railway Co. vs. Davidson, 257 U. S. 506 | 2, 7 |
| J. C. Penney Co. vs. Tax Commission, 238 Wis. 69 | 12 |
| Smietanka vs. First Trust and Savings Bank, 257 U. S. 602 | 2, 7 |
| The Montreal Mining Co. vs. Commissioner of Internal Revenue, 2 T. C. No. 85, Docket No. 106876 | 13 |
| Wisconsin vs. J. C. Penney Co., 311 U. S. 435..... | 4, 11, 12, 13 |
| Wisconsin Gas & Electric Co. vs. Wisconsin Tax Department, 243 Wis. 216..... | 14 |

Authorities—Continued.

Statutes Cited: (Federal)

| | Page |
|---|-----------------------|
| Judicial Code, Section 240 (a) | 2, 7 |
| Revenue Act of 1934, Section 23 (c) | 3, 4, 5, 8, 13, 14 |
| Revenue Act of 1934, Section 23 (d) | 3, 4, 5, 8, 9, 19, 21 |
| Revenue Act of 1936, Section 23 (c) | 13 |
| Revenue Act of 1928, Section 23 (c) (2) | 17 |

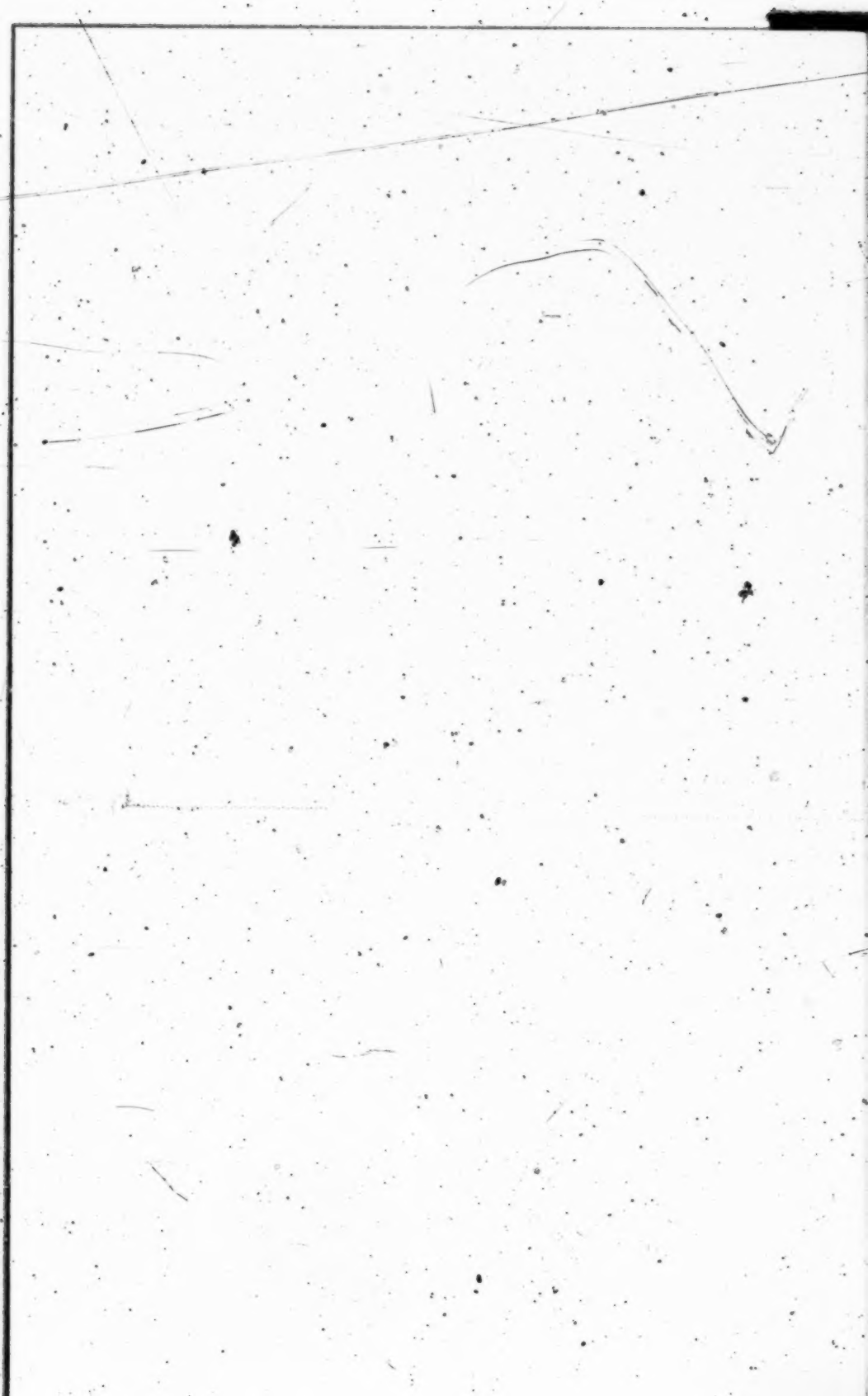
(Statutes and Acts of Wisconsin)

| | |
|---|-------|
| Laws of Wisconsin (1935) c. 505, Section 3, as amended by the Laws of Wisconsin (1935) c. 552, Sec. 1 | 3, 11 |
|---|-------|

| | |
|---|---------|
| Wisconsin State Income Tax Act (Section 71.03(4)) | 14, 18. |
|---|---------|

Other Authorities:

| | |
|--|----|
| The Restatement of the Law, Conflict of Laws, Section 42 (b) | 20 |
| Webster's New International Dictionary..... | 21 |



In the Supreme Court of the United States

No.

October Term, 1943

WISCONSIN GAS AND ELECTRIC COMPANY,

Petitioner,

vs.

THE UNITED STATES OF AMERICA.

**Petition for a Writ of Certiorari to the United States
Circuit Court of Appeals for the Seventh Circuit.**

**To the Honorable The Supreme Court of the United
States:**

The petitioner prays that a writ of certiorari issue to review the judgment entered November 8, 1943, in the United States Circuit Court of Appeals for the Seventh Circuit which reversed a judgment entered by the United States

District Court for the Eastern District of Wisconsin in favor of the petitioner.

OPINIONS BELOW.

The opinion of the Circuit Court of Appeals for the Seventh Circuit is reported in 138 F. (2d) 597. The opinion rendered by the District Court is reported in 46 Fed. Supp. 929. (R. 6, 20)

JURISDICTION.

The judgment of the Circuit Court of Appeals for the Seventh Circuit was entered November 8, 1943. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925, c. 229 (43 Stat. 938) (28 U. S. C. A. 347).

The cases believed to sustain said jurisdiction are as follows:

International Railway Co. vs. Davidson, 257 U. S. 506;

Smietanka vs. First Trust & Savings Bank, 257 U. S. 602 at P. 604.

SUMMARY STATEMENT.

In this suit under the Revenue laws to recover alleged excess income taxes paid by it for the year 1935 the petitioner taxpayer recovered judgment in the District Court of the United States for the Eastern District of Wisconsin. The issues presented to the Trial Court by the pleadings, (R. p. 2 to p. 4) and therein submitted upon an agreed statement of facts involved the validity of the action of the Commissioner of Internal Revenue in rejecting and disallowing petitioner's claim for refund premised upon the de-

ductibility, under Section 23 (c), (d) of the Revenue Act of 1934 of privilege dividend taxes paid by it to the State of Wisconsin for the year 1935. (R. 5)

The judgment of the District Court was founded upon Findings of Fact and Conclusions of Law made by the Court appropriate to a determination of the deductibility, for Federal tax purposes, of the privilege dividend tax paid to the State. (R. 9, 10)

Upon an appeal taken by the respondent from such adverse judgment to the United States Circuit Court of Appeals for the Seventh Circuit, that Court reversed the judgment of the District Court upon the issue of deductibility. (R. 20-23)

STATUTES INVOLVED.

The pertinent provisions of the Revenue Act of 1934, together with the provisions of the Wisconsin Privilege Dividend Tax (Laws of Wisconsin (1935), c. 505 Sec. 3, as amended by Laws of Wisconsin (1935), c. 552, Sec. 1) are printed in the Appendix, *infra* pp. 25, 23.

QUESTIONS PRESENTED.

1. Whether petitioner, a Wisconsin corporation engaged solely in the operation of public utilities within the State of Wisconsin and paying to that State, out of earnings from such public utility operations, pursuant to liability for payment imposed *solely* upon it under the Wisconsin privilege dividend tax law (Laws of Wisconsin (1935), c. 505, Sec. 3, as amended by Laws of Wisconsin (1935), c. 552, Sec. 1), taxes measured by the amount of dividends declared and paid to stockholders, may, for Federal income tax liability, and under Section 23 (c) of the Revenue Act of 1934, claim the amount of such exaction as

a deduction from gross income, notwithstanding the contention, in opposition to deductibility, that it did not bear the ultimate economic burden of the tax!

2. Whether the amount of the exaction from the petitioner by the State of Wisconsin for Wisconsin privilege dividend taxes should be allowed to the petitioner as a deduction under Sec. 23 (d) of the Revenue Act of 1934 as "taxes imposed upon a shareholder of the corporation upon his interest as shareholder which are paid by the corporation without reimbursement from the shareholder", if, notwithstanding the decisions of this Court and the Wisconsin Supreme Court holding the privilege dividend tax to be incident to corporate privileges and protection extended by the state, it is held that the tax is imposed upon the shareholder!

REASONS FOR GRANTING THE WRIT.

1. The decision of the Circuit Court of Appeals for the Seventh Circuit in construing Section 23 (c) of the Revenue Act of 1934, as denying to a Wisconsin corporation the right to deduct under Section 23 (c) the amount paid to the State of Wisconsin as a privilege dividend tax of that State unless such corporation could show that it bore the ultimate economic burden of such tax, is a decision of a Federal question in a way probably in conflict with applicable decisions of this Court, particularly those of *Wisconsin vs. J. C. Fenney Co.*, 311 U. S. 435 and *Biddle vs. Commissioner of Internal Revenue*, 302 U. S. 573, at P. 576.

2. If the decision of the Circuit Court of Appeals, holding that a Wisconsin corporation may not under Section 23 (c) of the Revenue Act of 1934, claim as a deduction the amount paid to the State of Wisconsin as a privilege

dividend tax of that State, can be construed as not in conflict with decisions of this Court, such decision then involves an important question of Federal law relating to the administration of the Internal Revenue Code which has not been, but which should be, decided by this Court.

3. If, notwithstanding the decisions of this Court and the Wisconsin Supreme Court holding the Privilege Dividend Tax to be incident to corporate privileges and protection extended by the State, it is determined that the tax is one imposed upon the shareholder and that no question of Federal law exists under Section 23 (c) of the Revenue Act of 1934, there remains an important question of Federal law relating to the administration of the Internal Revenue Code as to the deductibility of the tax under Section 23 (d) which has not been, but which should be, decided by this Court.

Wherefore, it is respectfully submitted that this petition should be granted.

VAN B. WAKE,
Attorney for Petitioner.

BRIEF IN SUPPORT OF PETITION.

OPINIONS.

One opinion was delivered by the District Court. It was written by District Judge F. Ryan Duffy and filed September 25, 1942. It appears on page 6 of the Record and is reported in 46 Fed. Supp. 929. The opinion of the Circuit Court of Appeals for the Seventh Circuit, (Circuit Judges J. Earl Major and Sherman Minton and District Judge Walter C. Lindley, Judge Minton writing) was filed November 8, 1943 and appears at page 20 of the Record. It is reported in 138 Fed. (2d) 597, advance sheets.

JURISDICTION.

The judgment of the Circuit Court of Appeals for the Seventh Circuit was entered November 8, 1943. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code.

Cases wherein jurisdiction was sustained for the purpose of review by certiorari in Internal Revenue matters are:

International Railway Co. vs. Davidson; 257 U. S. 506;
Smietanka vs. First Trust and Savings Bank, 257 U. S. 602, at P. 604.

SUMMARY STATEMENT.

This case was tried upon a stipulation for agreed statement of facts and the findings of fact filed by the District Court of the United States for the Eastern District of Wisconsin summarize the relevant matters. (R. 9) The petitioner is a Wisconsin corporation engaged in the operation

of public utilities wholly within the State of Wisconsin wherein it has its principal office. Out of the earnings attributable to such business, the petitioner made a declaration and payment of dividends in the year 1935, and in that year made payment to the State of Wisconsin, pursuant to the privilege dividend tax law of that State, of the sum of \$3,750.00, measured by the amount of the dividends declared and paid. The petitioner, by return based on the accrual method, claimed the amount of such payment as a deduction for that year for Federal income tax purposes under Section 23 (c) or (d) of the Revenue Act of 1934.

The Internal Revenue Agent disallowed such deduction and petitioner paid its tax liability in full without benefit of any deduction for the amount paid to the State of Wisconsin as privilege dividend tax. The petitioner, on May 9, 1939, timely filed with the Collector of Internal Revenue for the Eastern District of Wisconsin a claim for refund, inclusive of the tax resulting from the disallowed amount paid to the State of Wisconsin as privilege dividend tax. On October 31, 1940, the Commissioner of Internal Revenue rejected and disallowed the claim for refund and the petitioner, on February 19, 1941, filed suit in the District Court of the United States for the Eastern District of Wisconsin for recovery of the amount of tax specified in its claim for refund attributable to the amount paid to the State of Wisconsin as privilege dividend tax.

The District Court entered judgment in favor of the petitioner on October 6, 1942. Judgment of reversal was entered in the Circuit Court of Appeals for the Seventh Circuit on November 8, 1943, and it is such judgment that petitioner seeks to review.

SPECIFICATION OF ERRORS TO BE URGED.

The Court below erred:

1. In holding that the petitioner was foreclosed from deducting the amount paid as Wisconsin Privilege Dividend Tax because the Wisconsin Supreme Court had determined, for purposes of the State Income Tax Statute, that the economic burden of the tax was imposed upon the shareholders of petitioner.

2. In failing to recognize the petitioner's claim for deductibility of the tax under Section 23 (d) of the Revenue Act of 1934 if the tax was held to be one imposed upon shareholders.

SUMMARY OF ARGUMENT.

I.

The decision of the Circuit Court of Appeals decided a federal question in a way probably in conflict with applicable decisions of this Court.

Wisconsin vs. J. C. Penney Co., 311 U. S. 435.

The Federal question concerning the constitutional power of the State of Wisconsin to impose a privilege dividend tax upon a corporation has been determined in the affirmative by this Court. (Page 11)

The Wisconsin Supreme Court has consistently recognized that liability for such tax was imposed upon the corporation. (Page 12)

The holding of the Wisconsin Supreme Court that such tax is not deductible for purposes of the income tax laws of the state because the corporation paying the tax could not show that it bore the economic burden of the tax is not determinative of the Federal question now presented as to the deductibility of the

tax under Section 23 (c) of the Revenue Act. (Page 14)

To determine such Federal question upon the basis of the holding of the Wisconsin court, as was done by the Circuit Court of Appeals, would seem to be contrary to the principle of the *Biddle* case. (Page 14)

II.

The decision of the Circuit Court of Appeals involves an important question of federal law which should receive ultimate determination.

The Revenue Act is a self executing tax structure not dependent upon concepts from other tax systems. (Page 17)

III.

The decision of the Circuit Court of Appeals involves, but leaves unanswered, the alternative contention of the applicability of Section 23 (d) of the Revenue Act of 1934. Such proposition would appear to raise an important question of federal law not previously before this Court but worthy of final disposition.

If the tax presently involved is construed as one imposed upon the shareholder and not upon the corporation all the elements for deductibility under Section 23 (d) of the Revenue Act of 1934 are present and an important question of Federal law is before the Court. (Page 21)

A R G U M E N T .

I.

The decision of the Circuit Court of Appeals decided a federal question in a way probably in conflict with applicable decisions of this Court.

This Court has had previous occasion to consider the Wisconsin privilege dividend tax (Laws of Wisconsin (1935), c. 505, Section 3, as amended by the Laws of Wisconsin (1935), c. 552, Section 1); see Appendix, *infra* p. 23 for provisions of the Act. The Federal question concerning the constitutional power of the State of Wisconsin to impose such a tax was before this Court in *Wisconsin vs. J. C. Penney Co.*, 311 U. S. 435. A judgment of the Wisconsin Supreme Court was reversed on such Federal question.

In the present case the opinion of the Circuit Court of Appeals in reversal of the Trial Court recognized that reliance had been placed by the Trial Court upon such decision of this Court. Declining to follow that decision because it was thought by the Circuit Court of Appeals to be distinguishable on the facts from the instant case, the close parallel was, nevertheless, noted by the Court in the following language:

“The reasoning of that case would seem to sustain the District Court’s position. Power to tax was the only question before the court in the *Penney* case.
* * * (R. p. 23).

It is submitted that the language of the majority opinion of this Court in the case of *Wisconsin vs. J. C. Penney Co.*, 311 U. S. 435, in its affirmative determination of the power of the State to tax, justified the District Court in regarding the Wisconsin privilege dividend tax as one “* * * held * * * to be on the corporation and not upon the shareholders.” (R. 8)

Language from such majority opinion which seems singularly appropriate to the question of the imposition of the tax is the following:

" . . . The simple but controlling question is whether the state has given anything for which it can ask return. The substantial privilege of carrying on business in Wisconsin, which has here been given, clearly supports the tax, and the state has not given the less merely because it has conditioned the demand of the exaction upon happenings outside its own borders. The fact that a tax is contingent upon events brought to pass without a state does not destroy the nexus between such a tax and transactions within a state for which the tax is an exaction." *Wisconsin vs. J. C. Penney Co.*, 311 U. S. 435, at P. 444.

On remand, the Wisconsin Supreme Court (*J. C. Penney Co. vs. Tax Commission*, 238 Wis. 69, at P. 74) quoted such language as the basis on its own decision. The Wisconsin Court gave further confirmation to the theory that the validity of the tax rests upon the grant of the privilege of carrying on business in the corporate form within the State of Wisconsin by its decision in *International Harvester Co. vs. Department of Taxation*, 243 Wis. 198-205. Two portions of such opinion, respectively at pp. 205 and 206, are as follows:

" . . . If the term 'jurisdictional fact' must hereafter be relegated to the limbo of out-moded terms, the basis of Wisconsin's power to tax is the fact that it has given its protection and the benefits of government to corporate activities in Wisconsin and that profits from these activities are traceable to the fund from which dividends are paid. So far as the constitutional aspects of the cases are concerned, the federal supreme court has reduced the privilege features of the tax to mere conditions or contingencies, upon the happening of which the tax accrues." (Italics supplied)

.

" . . . We adhere to our determination upon remand of the *Penney* case, *supra*, that this is a *privilege tax* and that we are bound to accept the mandate of the United States supreme court that its constitutional justification from the standpoint of Wisconsin's power to tax is *the fact of net earnings in Wisconsin traceable to the fund distributed by the dividend.*" (Italics supplied)

The Tax Court of the United States also placed similar reliance upon language used in the case of *Wisconsin vs. J. C. Penney Co.*, 311 U. S. 435, in a case decided September 16, 1943. This was the case of *The Montreal Mining Co. vs. Commissioner of Internal Revenue*, 2 T. C. No. 85, Docket No. 106876, in which that court determined that amounts paid as Wisconsin Privilege Dividend Tax were deductible as taxes paid under Section 23 (c) of the Revenue Acts of 1934 and 1936. It was there said:

"The Supreme Court in *Wisconsin, et. al, vs. J. C. Penney Co.*, 311 U. S. 435, considered the Wisconsin Privilege Dividend Tax in connection with a constitutional question. In discussing the statute imposing such tax the Court said:

" . . . The practical operation of this legislation is to impose an additional tax on corporate earnings within Wisconsin but to postpone the liability for this tax until such earnings are paid out in dividends. In a word, by its general income tax Wisconsin taxes corporate income that is taken in; by the Privilege Dividend Tax of 1935 Wisconsin superimposed upon this income tax a tax on corporate income that is paid out."

Thus, it is apparent that the tax in question was there determined to be a levy on corporate income. Upon the authority of this decision, we hold in petitioner's favor on this issue. The tax is deductible under Section 23 (c) of the Revenue Acts of 1934 and 1936."

The Circuit Court of Appeals opinion in the instant case held against the deductibility of the Wisconsin Privilege Dividend Tax under Section 23 (c) of the Revenue Act of 1934 on the assumption that the Petitioner did not bear the economic burden of the tax, which factor it concluded was determinative of the issue. In the opinion reliance was placed upon two decisions of the Wisconsin Supreme Court, *Wisconsin Gas & Electric Company vs. Wisconsin Tax Department*, 243 Wis. 216, and *Blid vs. Wisconsin Foundry and Machine Co.*, 243 Wis. 221. In the latter case, decided upon a demurrer to the complaint, it was determined that a preferred stockholder could not recover from the corporation the amount it had withheld and paid to the state as privilege dividend tax for a dividend declared and paid. In the former case, the Wisconsin Supreme Court had for determination the question of the construction of the Wisconsin Income Tax Statute to determine whether or not the Privilege Dividend Tax was deductible thereunder.

Unlike Section 23 of the Revenue Act which authorizes the deduction of taxes paid with certain enumerated exceptions, the Wisconsin Statute authorizes only the deduction of enumerated taxes. Section 71.03 (4) of the Wisconsin Statutes, (set forth in Appendix, *infra* p. 26) in the authorization of the deduction of only specified taxes, includes "taxes paid during the year upon the business or property from which the income taxed is derived." The Wisconsin decisions relied upon by the Circuit Court of Appeals do not purport to decide the controlling Federal question.

The opinion of the Circuit Court of Appeals, predicated upon the determination of the Wisconsin Court for purposes solely associated with the state tax structure, of the question of the economic burden of the tax as distinguished

from legal liability for the tax, seems to be at variance with the decision of this Court in *Biddle vs. Commissioner of Internal Revenue*, 302 U. S. 573. In that case, American stockholders of a British corporation in reporting United States income taxes sought the right to deduct taxes paid to the British Government in respect of dividends declared. The Circuit Court of Appeals (C. C. A., 2nd), *Biddle vs. Commissioner*, 86 Fed. (2d) 718, held that the deduction could be taken only by the party liable for the payment of the tax without regard to its ultimate burden. Such determination was sustained on certiorari, *Biddle vs. Commissioner of Internal Revenue*, 302 U. S. 573. Several excerpts from the opinion on certiorari seem pertinent to the present Federal question:

"Section 131 does not say that the meaning of its words is to be determined by foreign taxing statutes and decisions, and there is nothing in its language to suggest that in allowing the credit for foreign tax payments, a shifting standard was adopted by reference to foreign characterizations and classifications of tax legislation. The phrase 'income taxes paid,' as used in our own revenue laws, has for most practical purposes a well understood meaning to be derived from an examination of the statutes which provide for the laying and collection of income taxes. It is that meaning which must be attributed to it as used in Section 131.

"Hence the board's finding, supported as it is by much expert testimony, that 'the stockholder receiving the dividend is regarded in the English income tax acts as having paid "by deduction or otherwise" the tax "appropriate" to the dividend' is not conclusive. At most it is but a factor to be considered in deciding whether the stockholder pays the tax within the meaning of our own statute. That must ultimately be determined by ascertaining from an examination of the manner in which the British tax is laid and collected what the stockholder has done in conformity to British law and whether it is

the substantial equivalent of payment of the tax as those terms are used in our own statute." (Page 578)

" . . . The corporation pays the standard tax and against it the remedies for non-payment run." (Page 579)

.

"Inclusion of the deducted amount in the base on which surtax is calculated, together with the provisions for refund of the tax to the stockholder who, in any event, bears its economic burden, are logical recognitions of the British conception that the standard tax paid by the corporation is passed on to the stockholders.

"Our revenue laws give no recognition to that conception. Although the tax burden of the corporation is passed on to its stockholders with substantially the same results to them as under the British system, our statutes take no account of that fact in establishing the rights and obligations of taxpayers. Until recently they have not laid a tax, except surtax, on dividends, but they have never treated the stockholder for any purpose as paying the tax collected from the corporation. Nor have they treated as taxpayers those upon whom no legal duty to pay the tax is laid. Measured by these standards our statutes afford no scope for saying that the stockholder of a British corporation pays the tax which is laid upon and collected from the corporation, and no basis for a decision that Section 131 extends to such a stockholder a credit for a tax paid by the corporation—a privilege not granted to stockholders in our own corporations. It can hardly be said that a tax paid to the Crown by a British corporation subject to United States income tax is not a tax paid within the meaning of Section 23 (c) (2), of the 1928 Act, which allows a deduction from gross income for taxes paid to a foreign country, cf. *Welch vs. St. Helens Petroleum Co.* (C. C. A. 9th), 78 F. (2d) 631, or that its stockholders could take credit under Section 131 for their share of the tax on the theory that they also had paid it." (Page 581)

The quoted language would seem to clearly recognize that a tax paid by a corporation under the law of its domicile and for which it was made liable would entitle the corporation to an equivalent deduction under Section 23 (c) of the 1928 Revenue Act, notwithstanding that the tax was upon the income received by the shareholder. Liability for the tax in the present case is imposed *solely* upon the corporation with no effort made by the Wisconsin Statute to impose either a contingent or secondary liability upon the shareholder. From the standpoint of legal liability, the shareholder enters the picture only by reason of the fact that the dividends received by him bear an arithmetical relationship to the tax liability of the corporation. The instant decision of the Circuit Court of Appeals certainly departed from the theory of such language and probably from the rule of law expressed therein.

II.

The decision of the Circuit Court of Appeals involves an important question of federal law which should receive ultimate determination.

If it can be rationally held that the decision of the Circuit Court of Appeals does not directly conflict with decisions of this Court, the discussion next above should serve to demonstrate that it appears dissonant with the rationale of such decisions. At no time have the decisions of the Wisconsin Supreme Court departed from the fundamental theory initially expounded by it in *State ex rel Froedert Grain & Malting Co. vs. Tax Commission*, 221 Wis. 225, at P. 245, that "Liability for payment of the tax is imposed upon the corporation." The uniform administrative practice of the State is to treat the corporation as the taxpayer and as the sole person liable for payment of the tax. (See

Appendix p. 26.) The determination by this Court of the Federal question in support of the power of the State to impose the Wisconsin Privilege Dividend Tax was adopted by the Wisconsin Supreme Court with appropriate compliance and without any effort to impinge upon the declared principle.

The State Court was still at liberty to determine the non-Federal question, in construing the Wisconsin State Income Tax Act, that taxes though based upon the grant of corporate privileges and for which the corporation only is made liable were not deductible under the Wisconsin State Income Tax Act because the ultimate economic burden was borne by the shareholder. Such is not the rule in respect of taxes deductible by a corporate taxpayer under Section 23 of the Revenue Act. The determination of the Wisconsin Court made no pretense of rendering a disposition of such Federal question. To import the reasoning of the Wisconsin Court into the present problem would seem to be introducing concepts of the Wisconsin system of taxation into the, otherwise, self executing Federal Revenue structure. Such a departure, if not in conflict with the principles announced by this Court in *Biddle vs. Commissioner of Internal Revenue*, 302 U. S. 573, would seem to present at least an important question of Federal law which should receive authoritative disposition with the objective of rendering clear the administration of the Internal Revenue Code.

III.

The decision of the Circuit Court of Appeals involves, but leaves unanswered, the alternative contention of the applicability of Section 23 (d) of the Revenue Act of 1934. Such proposition would appear to raise an important question of federal law not previously before this Court but worthy of final disposition.

Petitioner in Section V of its brief filed with the Circuit Court of Appeals asserted, as an alternative contention, that if it should be held that the Wisconsin Privilege Tax was imposed upon the shareholder it is, nevertheless, deductible under Section 23 (d) of the Revenue Act of 1934. The opinion of that Court makes no reference to such assertion. The mandate, however, is one of complete reversal of the judgment of the Trial Court. It would appear that such proposition has never before received the attention of this Court. A question of Federal law is involved which would seem to be of substantial importance to persons charged with the responsibility of administering the Revenue Act as well as to a considerable number of taxpayers. A final determination of the question would be of material assistance to the orderly application of the Federal tax structure.

Petitioner has heretofore endeavored to point out cogent reasons for regarding the tax involved herein as one imposed upon the corporation. If, however, it is determined that the tax is imposed upon the shareholder, its deductibility is claimed under Section 23 (d) of the Revenue Act of 1934 which admits of deduction "in case of taxes imposed upon a shareholder of a corporation upon his interest as shareholder which are paid by the corporation without reimbursement from the shareholder * * *".

Payment by petitioner as a corporation is admitted. If the tax is imposed upon a shareholder, it would seem to be "upon his interest as shareholder". Such expression would appear to include all of the rights inuring to a person by virtue of his holding stock including the right to dividends as an incident to the ownership thereof. The word "interest" is one of extremely broad import and it cannot be presumed that Congress intended its use in any narrow or restricted sense. The *Restatement of the Law, Conflict of Laws*, in Section 42 (b) defines interest to include "varying aggregates of rights, privileges, powers and immunities and distributively to mean any one of them".

There has been no reimbursement to the corporation from the shareholder and the theory of the economic incidence of the tax cannot reasonably be indulged in or used as a legal fiction to supply the element of reimbursement. The question of the economic incidence of a tax as between a shareholder and a corporation was discussed in the case of *Biddle vs. Commissioner of Internal Revenue*, 302 U. S. 573, and the following language was used at P. 580:

"Although the corporation, in the United Kingdom as here, pays the tax and is bound to pay it, the tax burden in point of substance is passed on to the stockholders in the same way that it is passed on under our own taxing acts where the tax on the corporate income is charged as an expense before any part of the resulting net profit is distributed to stockholders. See Magill, *Taxable Income*, 24 et seq. Whether the tax is deducted from gross profits before a dividend is declared, or after, when the deduction is taken from the gross dividend, the net amount received by the stockholder is the same. Under either system, if no dividend is declared no tax is paid by the stockholder. If a dividend is declared it must be paid, however the deduction is made, from what is left after the corporation has paid taxes upon its earnings * * *". (Page 580)

Reimbursement clearly connotes action of repayment made after an initial payment. Webster's new International Dictionary defines the word reimburse as meaning "to pay back; repay * * * to make restoration or payment of an equivalent to (a person)". The elements of deductibility under subsection (d) of Section 23 of the Revenue Act of 1934 seem to exist and if the tax presently involved is regarded as one imposed upon a shareholder an important question of Federal law is, nevertheless, before the Court.

CONCLUSION.

The decision of the Circuit Court of Appeals for the Seventh Circuit is in probable conflict with applicable decisions of this Court. If such decisions can be reconciled, the determination of the Circuit Court of Appeals presents an important question of Federal law not previously settled by this Court but justifying its intervention. The petitioner prays for the issuance of a writ of certiorari.

Respectfully submitted,

VAN B. WAKE,
Attorney for Petitioner,
773 North Broadway,
Milwaukee (2), Wisconsin

APPENDIX.

Wisconsin Privilege Dividend Tax.

Laws of Wisconsin (1935), c. 505, Sec. 3, as amended by Laws of Wisconsin (1935), c. 552, Sec. 1.

Section 3. *Privilege dividend tax.* (1) For the privilege of declaring and receiving dividends, out of income derived from property located and business transacted in this state, there is hereby imposed a tax equal to two and one-half per centum of the amount of such dividends declared and paid by all corporations (foreign and local), except those specified in paragraphs (d) and (g) of Section (1) of Section 71.05 of the Statutes, after the passage and publication of this act and prior to July 1, 1937. Such tax shall be deducted and withheld from such dividends payable to residents and non-residents by the payor corporation.

(2) Every corporation required to deduct and withhold any tax under this section shall, on or before the last day of the month following the payment of the dividend, make returns thereof and pay the tax to the tax commission, reporting such tax on the forms to be prescribed by the tax commission.

(3) Every such corporation hereby made liable for such tax, shall deduct the amount of such tax from the dividends so declared.

(4) In the case of corporations doing business within or without the state of Wisconsin, such tax shall apply only to dividends declared and paid out of income derived from business transacted and property located within the state of Wisconsin. The amount of income attributable to this state shall be computed in accordance with the

provisions of chapter 71. In the absence of proof to the contrary, such dividends shall be presumed to have been paid out of earnings of such corporation attributable to Wisconsin under the provisions of chapter 71, for the year immediately preceding the payment of such dividend. If a corporation had a loss for the year prior to the payment of the dividend, the tax commission shall, upon application, determine the portion of such dividend paid out of corporate surplus and undivided profits derived from business transacted and property located within the state.

(5) Dividends paid by a subsidiary corporation to its parent shall not be subject to the tax herein imposed provided that the subsidiary and its parent report their income for taxation under the provisions of chapter 71 on a consolidated income return basis, or both corporations report separately.

(6) The provisions of this section shall not apply to dividends declared and paid by a Wisconsin corporation out of its income which it has reported for taxation under the provisions of chapter 71, if the business of such corporation consists in the receipt of dividends and the distribution thereof to its stockholders.

(7) For the purposes of this section dividends shall be defined as in section 71.02, except that the tax herein imposed shall not apply to stock dividend or liquidating dividends.

(8) The tax hereby levied, if not paid within the time herein provided, shall become delinquent and when delinquent shall be subject to a penalty of two per cent on the amount of the tax and interest at the rate of one-half per cent per month until paid.

(9) The tax hereby imposed shall, when collected by the tax commission, be paid by it into the state treasury.

Extract from the Revenue Act of 1934.

"Sec. 23. Deductions from gross income.

In computing net income there shall be allowed as deductions:

(a) Expenses. . . .

(b) Interest. . . .

(c) Taxes Generally. Taxes paid or accrued within the taxable year, except—

(1) Federal income, war-profits, and excess-profits taxes;

(2) income, war-profits, and excess-profits taxes imposed by the authority of any foreign country or possession of the United States; but this deduction shall be allowed in the case of a taxpayer who does not signify in his return his desire to have to any extent the benefits of section 131 (relating to credit for taxes of foreign countries and possessions of the United States);

(3) estate, inheritance, legacy, succession, and gift taxes; and

(4) taxes assessed against local benefits of a kind tending to increase the value of the property assessed; but this paragraph shall not exclude the allowance as a deduction of so much of such taxes as is properly allocable to maintenance or interest charges.

(d) *Taxes of shareholder paid by corporation.* — The deduction for taxes allowed by subsection (c) shall be allowed to a corporation in the case of taxes imposed upon a shareholder of the corporation upon his interest as shareholder which are paid by the corporation without reimbursement from the shareholder, but in such cases no deduction shall be allowed the shareholder for the amount of such taxes."

**Section 71.03 (4) of the Wisconsin Statutes dealing
with Wisconsin Income Taxes.**

“71.03 Deductions from gross income of corporations. Every corporation, joint stock company or association shall be allowed to make from its gross income the following deductions:

(4) Taxes other than special improvement taxes paid during the year upon the business or property from which the income taxed is derived, including therein taxes imposed by the state of Wisconsin and the government of the United States as income, excess or war profits and capital stock taxes, including taxes on real property which is owned and held for business purposes whether income producing or not, provided that such portion of the deduction for federal income and excess profits taxes as may be allowable shall be confined to cash payments made within the year covered by the income tax return, and provided further that deductions for income taxes paid to the United States government shall be limited to taxes paid on net income which is taxable under this chapter; and provided further that income taxes imposed by the state of Wisconsin shall accrue for the purpose of this subsection only in the year in which such taxes are assessed.” (Wis. Statutes, 1935)

**Administrative practice concerning Wisconsin
Privilege Dividend Tax.**

“By order of the Wisconsin Tax Commission, corporations were advised March 4, 1938, that ‘Wisconsin privilege dividend taxes levied pursuant to Sec. 3, Ch. 505, Laws of 1935, as amended, whether deducted from dividends paid to stockholders or assumed by corporation without deduction from dividends paid to stockholders, are to be computed at a rate of 2 1/2%’. (Prentice-Hall, State and Local Tax Service—Wisconsin, Section 13,288).

In *Household Finance Corp. vs. Department of Taxation*, the Wisconsin Board of Tax Appeals determined a stockholder may not petition for abatement of privilege dividend tax paid by a corporation as the corporation is the aggrieved taxpayer, not the stockholder. (Prentice-Hall, State and Local Tax Service, Wisconsin, Section 13,616).

In a letter from the Wisconsin Tax Commission by T. Carroll Sizer, attorney, dated April 21, 1936, it is stated that the privilege dividend tax is defined to be an excise tax levied in respect of the declaration and payment of dividends rather than a tax on the receipt of income. (Prentice-Hall, State and Local Service, Wisconsin, Section 13,207).

Comet Co. vs. Department of Taxation, 243 Wis. 117, where the court said:

‘As in the absence of that provision (an amendment) Comet, as a Wisconsin corporation, *would be liable* for the privilege dividend tax of two and one-half per cent *imposed by the act* upon all dividends distributed by it to its stockholders’ (Page 123) (Emphasis supplied)

INDEX

| | Page |
|--------------------------------|------|
| Opinions Below | 1 |
| Jurisdiction | 2 |
| Questions Presented | 2 |
| Summary Statement | 3 |
| Specifications of Errors | 5 |
| Statutes Involved | 5 |
| Summary of Argument | 5 |

Argument:

- I. The Wisconsin Privilege Dividend Tax is payable by the corporation and is collectible from it only. The usual incidents of tax liability arising from it devolve upon the corporation. The ultimate economic burden of the tax is not important under Section 23 of the Revenue Act of 1934 8
- II. The privilege dividend tax as a payment exacted from the corporation based upon the privileges extended and protection given by the State to the corporate enterprise, and measured by the exercise of a function necessary to corporate existence, is deductible if it otherwise meets the requirements of Section 23 of the Revenue Act of 1934 24
- III. Subsequent decisions of the Wisconsin Supreme Court have not changed the status of the privilege dividend tax as it existed at the time of the Trial Court's decision 27
- IV. Regulations as between corporation and shareholder imposed by the state of Wisconsin in the exercise of its power over corporations domiciled in the state or foreign corporations licensed therein have no more effect on the status of the

Argument—Continued.

| | Page |
|--|------|
| tax payment under federal law than a contractual arrangement for the sharing of the tax burden | 31 |
| V. If, notwithstanding the decisions of the Wisconsin Supreme Court and the Federal Supreme Court holding the privilege dividend tax to be incident to corporate privileges and protection extended by the state it is held that the tax is imposed upon the shareholder, it is still deductible under Section 23 (d) of the Revenue Act of 1934 | 33 |
| Conclusion | 36 |

APPENDIX:

| | |
|--|----|
| Wisconsin Privilege Dividend Tax | 39 |
| Extract from Section 23 of the Revenue Act of 1934 | 41 |

AUTHORITIES.

Cases Cited:

| | |
|---|--------------------|
| Biddle vs. Commissioner of Internal Revenue, 302 U. S. 573 | 19, 21, 23, 24, 35 |
| 86 Fed. (2d) 718 | 20 |
| Blid vs. Wisconsin Foundry and Machinery Co., 243 Wis. 221 | 15, 16, 28 |
| Carpenter vs. Shaw, 280 U. S. 363 | 29 |
| Central Bank vs. United States, 137 U. S. 355 | 30 |
| Comet vs. Department of Taxation, 243 Wis. 117 | 10 |

Authorities—Continued.

| | Page |
|--|---------------|
| Connecticut Gen. Lia. Ins. Co. vs. Johnson, 303 U. S. 77 | 11, 27 |
| Dobson vs. Commissioner of Internal Revenue, U. S., 88 L. Ed. Adv. Op. 179 | 14 |
| Eastern Gas & Fuel Association vs. Commission- er, 128 Fed. (2d) 369 (C. C. A. 1st) | 9, 25, 31, 34 |
| Falk Corp. vs. Commissioner, 60 Fed. (2d) 204 (C. C. A. 7th) | 25 |
| Froedtert Grain & Malting Co. St., ex rel vs. Tax Commission, 221 Wis. 225 | 9 |
| Household Finance Corp. vs. Department of Tax- ation, Prentice-Hall, State and Local Tax Service, Wisconsin, Section 13,616 | 10 |
| International Harvester Co. vs. Wisconsin De- partment of Taxation, 243 Wis. 198 | 12, 28 |
| International Railway Co. vs. Davidson, 257 U. S. 506 | 2 |
| Keith vs. Johnson, 271 U. S. 1 | 18 |
| Magruder vs. Supplee, 316 U. S. 394 | 25 |
| Missouri ex rel S. W. Bell Tel. Co. vs. Public Service Commission, 262 U. S. 276 | 25 |
| National Bank of Commerce vs. Allen, 223 Fed. 472 (C. C. A. 8th) | 30 |
| New Jersey vs. Anderson, 203 U. S. 483 | 29 |
| New York, Philadelphia & Norfolk Tel. Co. vs. Dolan, 265 U. S. 96 | 29 |

Authorities—Continued.

| | Page |
|---|------|
| Northwest Engineering Corp. vs. Department of Taxation, 241 Wis. 324 | 26 |
| J. C. Penney Co. vs. Tax Commission, 233 Wis. 286 11, 26-27, 36 238 Wis. 69 12, 27, 28 | |
| Rogers vs. Guaranty Trust Co., 288 U. S. 123 | 31 |
| Schuylkill Trust Co. vs. Pennsylvania, 296 U. S. 113 29 302 U. S. 506 31 | |
| Shearer vs. Commissioner, 48 Fed. (2d) 552 (C. C. A. 2nd) | 25 |
| Smietanka vs. First Trust and Savings Bank, 257 U. S. 602 | 2 |
| Starbuck's Executrix, 251 N. Y. 439 | 34 |
| State Tax Comm. of Utah vs. Aldrich, 316 U. S. 174-181 | 31 |
| Stewart Dry Goods Co. vs. Lewis, 294 U. S. 550 | 29 |
| The Montreal Mining Co. vs. Commissioner of Internal Revenue, 2 T. C. No. 85, Docket No. 106876 | 13 |
| Travis vs. Yale & Towne Mfg. Co., 252 U. S. 60 | 10 |
| United States vs. Mitchell, 271 U. S. 9 | 19 |
| United States vs. Woodward, 256 U. S. 632 | 18 |
| Vieux vs. Sixth Ward Building & Loan Associa- tion, 310 U. S. 32 | 31 |
| Wisconsin vs. J. C. Penney Co., 311 U. S. 435 8, 11, 13, 24, 26 | |

Authorities—Continued.

Page

| | |
|---|----------------|
| Wisconsin Gas & Electric Company vs. Department of Taxation, 243 Wis. 216 | 15, 16, 17, 28 |
| F. W. Woolworth Co. vs. United States, 91 Fed. (2d) 973 (certiorari denied), 302 U. S. 768 | 20 |

Statutes Cited (Federal):

| | |
|---|---------------|
| Judicial Code, Section 240 (a) | 2 |
| Revenue Act of 1928, Section 23 (c) (2) | 23 |
| Revenue Act of 1934, Section 23 (c) | 2, 15 |
| Section 23 (d) | 3, 33, 34, 35 |
| Revenue Act of 1936, Section 23 (c) | 13 |
| Title VII | 18 |
| Motor Vehicle Excise Tax, (Sec. 900, Laws of 1921) | 25 |

Wisconsin Statutes:

| | |
|--|------------|
| Section 71.03 (4) (1935) | 15, 17, 28 |
| Laws of 1935, Chapter 505, Section 3 | 2, 5, 8 |
| Chapter 552, Section 1 | 2, 5, 8 |
| Wisconsin Constitution, Section 1, Article XI | 31 |

Other Authorities:

| | |
|--|--------|
| Wisconsin State Income Tax Act..... | 15, 41 |
| Prentice-Hall, State and Local Tax Service, Wisconsin, Section 13,207 | 10 |
| Section 13,616 | 10 |
| Section 13,288 | 10, 32 |

Authorities—Continued.

| | Page |
|---|------|
| Restatement of the Law, Conflict of Laws, Section 42 (b) | 34 |
| Webster's New International Dictionary | 36 |
| I. T. 3191, C. B. 1938-1, page 143 | 25 |
| I. T. 3378, C. B. 1940-1, page 36 | 26 |

In the Supreme Court of the United States

No. 565

October Term, 1943

WISCONSIN GAS AND ELECTRIC COMPANY,

Petitioner,

vs.

THE UNITED STATES OF AMERICA.

**On Writ of Certiorari to the
United States Circuit Court of Appeals for the Seventh Circuit.**

BRIEF FOR THE PETITIONER

OPINIONS.

One opinion was delivered by the District Court. It was written by District Judge F. Ryan Duffy and filed September 25, 1942. It appears on page 6 of the Record and is reported in 46 Fed. Supp. 929. The opinion of the

Circuit Court of Appeals for the Seventh Circuit, (Circuit Judges J. Earl Major and Sherman Minton and District Judge Walter C. Lindley, Judge Minton writing) was filed November 8, 1943, and appears at page 20 of the Record. It is reported in 138 Fed. (2d) 597, advance sheets.

JURISDICTION.

A petition for writ of certiorari herein was granted by this Court on January 31, 1944 and the case was transferred to the summary docket.

The judgment of the Circuit Court of Appeals for the Seventh Circuit was entered November 8, 1943. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code.

Cases wherein jurisdiction was sustained for the purpose of review by certiorari in Internal Revenue matters are:

International Railway Co. vs. Davidson, 257 U. S. 506;

Smietanka vs. First Trust and Savings Bank, 257 U. S. 602, at p. 604.

QUESTIONS PRESENTED.

1. Whether petitioner, a Wisconsin corporation engaged solely in the operation of public utilities within the State of Wisconsin and paying to that State, out of earnings from such public utility operations, pursuant to liability for payment imposed *solely* upon it under the Wisconsin privilege dividend tax law (Laws of Wisconsin (1935), c. 505, Sec. 3, as amended by Laws of Wisconsin (1935), c. 552, Sec. 1), taxes measured by the amount of dividends declared and paid to stockholders, may, for Federal income tax liability, and under Section 23 (c) of the

Revenue Act of 1934, claim the amount of such charge as a deduction from gross income, notwithstanding the contention, in opposition to deductibility, that it did not bear the ultimate economic burden of the tax?

2. Whether the amount of the payment from the petitioner to the State of Wisconsin for Wisconsin privilege dividend taxes should be allowed to the petitioner as a deduction under Sec. 23 (d) of the Revenue Act of 1934 as "taxes imposed upon a shareholder of the corporation upon his interest as shareholder which are paid by the corporation without reimbursement from the shareholder", if, notwithstanding the decisions of this Court and the Wisconsin Supreme Court holding the privilege dividend tax to be incident to corporate privileges and protection extended by the state, it is held that the tax is imposed upon the shareholder?

SUMMARY STATEMENT.

This case was tried upon a stipulation for agreed statement of facts and the findings of fact filed by the District Court of the United States for the Eastern District of Wisconsin summarize the relevant matters. (R. 9) The petitioner is a Wisconsin corporation engaged in the operation of public utilities wholly within the State of Wisconsin wherein it has its principal office. Out of the earnings attributable to such business, the petitioner made a declaration and payment of dividends in the year 1935, and in that year made payment to the State of Wisconsin pursuant to the privilege dividend tax law of that State, of the sum of \$3,750.00, measured by the amount of the dividends declared and paid. The petitioner, by return based on the accrual method, claimed the amount of such payment as a deduction for that year for Federal income tax purposes under Section 23 (c) or (d) of the Revenue Act of 1934.

The Internal Revenue Agent disallowed such deduction and petitioner paid its tax liability in full without benefit of any deduction for the amount paid to the State of Wisconsin as privilege dividend tax. The petitioner, on May 9, 1939, timely filed with the Collector of Internal Revenue for the Eastern District of Wisconsin a claim for refund, inclusive of the tax resulting from the disallowed amount paid to the State of Wisconsin as privilege dividend tax. On October 31, 1940, the Commissioner of Internal Revenue rejected and disallowed the claim for refund and the petitioner, on February 19, 1941, filed suit in the District Court of the United States for the Eastern District of Wisconsin for recovery of the amount of tax specified in its claim for refund attributable to the amount paid to the State of Wisconsin as privilege dividend tax.

The District Court entered judgment in favor of the petitioner on October 6, 1942. Judgment of reversal was entered in the Circuit Court of Appeals for the Seventh Circuit on November 8, 1943, and it is such judgment that petitioner seeks to review.

As indicated by the opinion of the trial court, the question for decision is the petitioner's right to the deduction of privilege dividend taxes paid to the State of Wisconsin during the taxable year (R. 7). The Government asserted before the trial court and in its brief in the Circuit Court of Appeals that the tax was not paid by the corporation but by the shareholders and, accordingly, the amount paid was not deductible by the corporation under Section 23 of the Revenue Act of 1934. The Government's contention was rejected by the trial court but adopted by the Circuit Court of Appeals for the Seventh Circuit (R. 22).

SPECIFICATION OF ERRORS TO BE URGED.

The Court below erred:

1. In holding that the petitioner was foreclosed from deducting from gross income, in the computation of Federal Income tax liability, the amount paid as Wisconsin Privilege Dividend Tax because the Wisconsin Supreme Court had determined, for purposes of the State Income Tax Statute, that the economic burden of the tax was imposed upon the shareholders of petitioner.

2. In failing to recognize the petitioner's claim for deductibility of the tax under Section 23 (d) of the Revenue Act of 1934 if the tax was held to be one imposed upon shareholders.

STATUTES INVOLVED.

The pertinent provisions of the Revenue Act of 1934 (Sec. 23), together with the provisions of the Wisconsin Privilege Dividend Tax (Laws of Wisconsin (1935), c. 505 Sec. 3, as amended by Laws of Wisconsin (1935), c. 552, Sec. 1) are printed in the Appendix, *infra* pp. 41, 39.

SUMMARY OF ARGUMENT.

I.

The Wisconsin Privilege Dividend Tax is payable by the corporation and is collectible from it only. The usual incidents of tax liability arising from it devolve upon the corporation. The ultimate economic burden of the tax is not important under Section 23 of the Revenue Act of 1934.

Both the Statute and the state administrative practice thereunder treat the corporation as the taxpayer. (p. 9)

The Wisconsin Court has confirmed the theory that the validity of the tax rests upon privileges granted by the State to the corporation. (p. 12)

Both the Trial Court and the Tax Court regarded the tax as deductible under Section 23 of the Revenue Act. (p. 13)

The Wisconsin decisions relied upon by the Circuit Court of Appeals determined only the question of State law and not the instant controversy. (p. 15)

The rule announced by the Wisconsin Court concerning deductibility does not appear to be consonant with the federal rule. (p. 17)

II.

The Privilege Dividend Tax, as a payment exacted from the corporation based upon the privileges extended and protection given by the state to the corporate enterprise, and measured by the exercise of a function necessary to corporate existence, is deductible if it otherwise meets the requirements of Section 23 of the Revenue Act of 1934.

The payment of the dividend tax by a corporation is made under the compulsion of the Statute and arises as an incident to the exercise of a vital corporate function. (p. 25)

III.

Subsequent decisions of the Wisconsin Supreme Court have not changed the status of the Privilege Dividend Tax as it existed at the time of the trial court's decision.

The Wisconsin Court by subsequent decisions has merely determined, for state purposes, that the economic burden of the tax is passed on to shareholders. (p. 28)

IV.

Regulations as between corporation and shareholder imposed by the state of Wisconsin in the exercise of its power over corporations domiciled in the state or foreign corporations licensed therein have no more effect on the status of the tax payment under federal law than a contractual arrangement for the sharing of the tax burden.

The economic burden of all corporate taxes would seem to fall upon the shareholder, and hence a state regulation between the corporation and shareholder which asserts the final incidence of a tax is immaterial to the present controversy. (p. 32)

V.

If notwithstanding the decisions of the Wisconsin Supreme Court and the Federal Supreme Court holding the Privilege Dividend Tax to be incident to corporate privileges and protection extended by the state, it is held that the tax is imposed upon the shareholder, it is still deductible under Section 23 (d) of the Revenue Act of 1934.

If the tax is one imposed upon a shareholder, it appears to be imposed upon his interest as shareholder. (p. 35)

If the tax is one imposed upon a shareholder, it would seem that the other necessary elements for deductibility under Section 23 (d) are present. (p. 36)

Argument.

I.

The Wisconsin Privilege Dividend Tax is payable by the corporation and is collectible from it only. The usual incidents of tax liability arising from it devolve upon the corporation. The ultimate economic burden of the tax is not important under Section 23 of the Revenue Act of 1934.

This Court has had previous occasion to consider the Wisconsin privilege dividend tax (Laws of Wisconsin (1935), c. 505, Section 3, as amended by the Laws of Wisconsin (1935), c. 552, Section 1); see Appendix, *infra* p. 39 for provisions of the Act. The Federal question concerning the constitutional power of the State of Wisconsin to impose such a tax was before this Court in *Wisconsin vs. J. C. Penney Co.*, 311 U. S. 435. A judgment of the Wisconsin Supreme Court was reversed on such Federal question.

The petitioner claims the right to deduct under Section 23 of the Revenue Act of 1934 (Appendix, *infra* p. 41) the amount of such tax paid in 1935.

The privilege dividend statute effective in the year 1935 provides:

"For the *privilege* of declaring and receiving dividends out of income derived from property located and business transacted in this state there is hereby imposed a tax * * *." (Italics supplied)

When a dividend is lawfully declared it becomes a debt. While the statute refers to the "privilege of declaring and receiving dividends", the privilege of receiving is purely derivative and involves no legislative indulgence to the shareholder.¹

¹ See paragraph 3 of footnote page 10, *infra*.

By Subsection (2) every corporation is required to deduct the tax, make returns thereof and *pay* the tax to the Tax Commission.

By Subsection (3) it is provided:

"Every such corporation hereby made liable for the tax shall deduct the amount of such tax from the dividend so declared."

Provision is made in Subsection (4) for the apportionment of the tax in respect of corporations doing business within and without the state so that the privilege dividend tax shall relate only to dividends paid out of corporate surplus and undivided profits derived from business transacted and property located within the state.

By Subsection (5) dividends paid by a subsidiary to a parent corporation are not subject to the tax.

By Subsection (6) the tax is not applicable to dividends declared and paid by Wisconsin corporations out of income reported for taxation to the state if the business of the corporation consists in the receipt and distribution of dividends.

By Subsection (7) the privilege dividend tax is not applicable to stock dividends or liquidating dividends.

Subsection (8) provides that the tax if not paid within the time provided shall become delinquent and the delinquent shall be subject to penalty.

No provision is made in the Act for payment by the shareholder or enforcement of collection from the shareholder. The tax, unlike that involved in *Eastern Gas & Fuel Association vs. Commissioner*, 128 Fed. (2d) 369 (C. C. A. 1st) is not a general tax upon income of shareholders in common with the recipients of income from other sources.

In *Froedtert Grain & Malting Co. vs. Tax Commission*, 221 Wis. 225, the court said at page 245:

"Liability for payment of the tax is imposed upon the corporation."

In the same case at page 237 the court, referring to *Travis vs. Yale & Towne Mfg. Co.*, 252 U. S. 60, said:

"Upon like reason the instant tax may be considered as in effect imposed against the corporation."

The uniform administrative practice is to treat the corporation as the taxpayer and as the sole person liable for payment of the tax.¹

¹ By order of the Wisconsin Tax Commission, corporations were advised March 4, 1938, that "Wisconsin privilege dividend taxes levied pursuant to Sec. 3, Ch. 505, Laws of 1935, as amended, whether deducted from dividends paid to stockholders or assumed by corporation without deduction from dividends paid to stockholders, are to be computed at a rate of 2 1/2%." (Prentice-Hall, State and Local Tax Service—Wisconsin, Section 13,288.)

In *Household Finance Corp. vs. Department of Taxation*, the Wisconsin Board of Tax Appeals determined a stockholder may not petition for abatement of privilege dividend tax paid by a corporation as the corporation is the aggrieved taxpayer, not the stockholder. (Prentice-Hall, State and Local Tax Service, Wisconsin, Section 13,616.)

In a letter from the Wisconsin Tax Commission by T. Carroll Sizer, attorney, dated April 21, 1936, it is stated that the privilege dividend tax is defined to be an excise tax levied in respect of the declaration and payment of dividends rather than a tax on the receipt of income. (Prentice-Hall, State and Local Service, Wisconsin, Section 13,207.)

Comet Co. vs. Dept. of Taxation, 243 Wis. 117, where the court said:

"As in the absence of that provision [an amendment] Comet, as a Wisconsin corporation, would be liable for the privilege dividend tax of two and one-half per cent imposed by the act upon all dividends distributed by it to its stockholders * * *." (Page 123) (Emphasis supplied)

In *J. C. Penney Co. vs. Tax Commission*, 233 Wis. 286, the court declared at page 292:

" * * * It is agreed on all sides that the tax in question is an excise tax and this court so held in the *Froedtert* case. The Court in effect held that the tax was an excise tax—

'for the privilege of declaring and receiving dividends out of income derived from property located and business transacted in this state,'—

and was therefore subject to the jurisdiction of the state as are incomes and inheritances. It is apparent that upon this basis the tax imposed by sub. (1) of sec. 3 of the act, cannot be imposed upon dividends declared by a foreign corporation because they are not declared within this state nor is the privilege one granted by this state."

In the *Penney* case, the Wisconsin Court under the supposed compulsion of the decision of this Court in *Connecticut Gen. L. Ins. Co. vs. Johnson*, 303 U. S. 77, held the tax invalid as to dividends declared outside the State by a foreign corporation. The State obtained review by this Court and upon such review, *Wisconsin vs. J. C. Penney Co.*, 311 U. S. 435, this Court reversed by 5 to 4 decision. In the majority opinion (page 444), it was said:

" * * * The simple but controlling question is whether the state has given anything for which it can ask return. The substantial privilege of carrying on business in Wisconsin, which has here been given, clearly supports the tax, and the state has not given the less merely because it has conditioned the demand of the exaction upon happenings outside its own borders. The fact that a tax is contingent upon events brought to pass without a state does not destroy the nexus between such a tax and transactions within a state for which the tax is an exaction."

The minority opinion (page 449) asserted that as the burden of the tax was on the shareholders and Wisconsin

is powerless to tax the incomes of non-resident shareholders, the Statute applied to dividends of foreign corporations declared outside of the state and paid to non-resident shareholders should be condemned.

On remand the Wisconsin Supreme Court (*J. C. Penney Co. vs. Tax Commission*, 238 Wis. 69) quoted the above designated language of the majority opinion of this Court as the basis of its own decision. The Wisconsin Court gave further confirmation to the theory that the validity of the tax rests upon the grant of the privilege of carrying on business in the corporate form within the State of Wisconsin by its decision in *International Harvester Co. vs. Department of Taxation*, 243 Wis. 198-205, where the Court said:

“ . . . If the term ‘jurisdictional fact’ must hereafter be relegated to the limbo of outmoded terms, *the basis of Wisconsin’s power to tax is the fact that it has given its protection and the benefits of government to corporate activities in Wisconsin and that profits from these activities are traceable to the fund from which dividends are paid. So far as the constitutional aspects of the cases are concerned, the federal supreme court has reduced the privilege features of the tax to mere conditions or contingencies, upon the happening of which the tax accrues.*” (Page 205) (Italics supplied)

The court says further on page 206:

“ . . . We adhere to our determination upon remand of the Penney case, *supra*, that this is a privilege tax and that we are bound to accept the mandate of the United States supreme court that its constitutional justification from the standpoint of Wisconsin’s power to tax is the fact of net earnings in Wisconsin traceable to the fund distributed by the dividend.” (Italics supplied)

“ . . . Sec. 3 of sec. 71.60, Stats., provides without qualification that the tax shall be levied for the privilege of declaring and receiving dividends out

of income derived from property located and business transacted in this state." (page 206)

In the present case, the opinion of the Circuit Court of Appeals in reversal of the Trial Court recognizes that reliance had been placed by the Trial Court upon the decision of this Court in the *Penney* case. Declining to follow that decision because it was thought by the Circuit Court of Appeals to be distinguishable on the facts from the instant case, the close parallel was, nevertheless, noted by the Court below in the following language:

"The reasoning of that case would seem to sustain the District Court's position. Power to tax was the only question before the Court in the *Penney* case (R. 23)."

It is submitted that the language of the majority opinion of this Court in the case of *Wisconsin vs. J. C. Penney Co.*, 311 U. S. 435, in its affirmative determination of the power of the State to tax, justified the District Court in regarding the Wisconsin Privilege Dividend Tax as one " . . . held . . . to be on the corporation and not upon the shareholders". (R. 8)

The Tax Court of the United States in a case decided September 16, 1943, also placed similar reliance upon language used in the majority opinion of this Court in the *Penney* case.

This was the case of *The Montreal Mining Co. vs. Commissioner of Internal Revenue*, 2 T. C. No. 85, Docket No. 106876, in which that court determined that amounts paid as Wisconsin Privilege Dividend Tax were deductible as taxes paid under Section 23 (c) of the Revenue Acts of 1934 and 1936. It was there said:

"The Supreme Court in *Wisconsin, et al, vs. J. C. Penney Co.*, 311 U. S. 435, considered the Wisconsin Privilege Dividend Tax in connection with a consti-

tutional question. In discussing the statute imposing such tax the Court said:

“ * * * The practical operation of this legislation is to impose an additional tax on corporate earnings within Wisconsin but to postpone the liability for this tax until such earnings are paid out in dividends. In a word, by its general income tax Wisconsin taxes corporate income that is taken in; by the Privilege Dividend Tax of 1935 Wisconsin superimposed upon this income tax a tax on corporate income that is paid out.”

Thus, it is apparent that the tax in question was there determined to be a levy on corporate income. Upon the authority of this decision, we hold in petitioner's favor on this issue. The tax is deductible under Section 23 (c) of the Revenue Acts of 1934 and 1936.”

That special importance should be attached to decisions of the Tax Court was recognized by this Court in the case of *Dobson vs. Commissioner of Internal Revenue*, U. S., 88 Law. Ed. Advance Opinions, 179. High tribute was paid in such opinion to the qualifications and attributes of the Tax Court concerning its ability, methods, and presumptive likelihood of rendering fair and accurate decisions. Concerning the rendition of such decisions involving questions of law, the following was there said (page 187) concerning the Tax Court:

“In deciding law questions courts may properly attach weight to the decision of points of law by an administrative body having special competence to deal with the subject matter. The Tax Court is informed by experience and kept current with tax evolution and needs by the volume and variety of its work. While its decisions may not be binding precedents for courts dealing with similar problems, uniform administration would be promoted by conforming to them where possible.”

The Circuit Court of Appeals opinion in the instant case held against the deductibility of the Wisconsin Privilege Dividend Tax under Section 23 (c) of the Revenue Act of 1934 on the assumption that the Petitioner did not bear the economic burden of the tax, which factor it concluded was determinative of the issue. In the opinion reliance was placed upon two decisions of the Wisconsin Supreme Court, *Wisconsin Gas & Electric Company vs. Wisconsin Tax Department*, 243 Wis. 216, and *Blid vs. Wisconsin Foundry and Machine Co.*, 243 Wis. 221. In the latter case, decided upon a demurrer to the complaint, it was determined that a preferred stockholder could not recover from the corporation the amount it had withheld and paid to the state as privilege dividend tax for a dividend declared and paid. In the former case, the Wisconsin Supreme Court had for determination the question of the construction of the Wisconsin Income Tax Statute to determine whether or not the Privilege Dividend Tax was deductible thereunder.

Unlike Section 23 of the Revenue Act which authorizes the deduction of taxes paid with certain enumerated exceptions, the Wisconsin Statute authorizes only the deduction of enumerated taxes. Section 71.03 (4) of the Wisconsin Statutes,¹ in the authorization of the deduction of only specified taxes, includes "taxes paid during the year upon the business or property from which the income taxed is derived." The Wisconsin decisions relied upon by the Circuit Court of Appeals do not purport to decide the controlling Federal question.

¹ "71.03 Deductions from gross income of corporations. Every corporation, joint stock company or association shall be allowed to make from its gross income the following deductions:

(Continued on next page)

Nothing said by the Wisconsin Court in either of the last above mentioned decisions purports to alter its prior pronouncement, in conformity with the determination of this Court, that the tax is reciprocal to and grounded upon corporate privileges extended by the state. In *Wisconsin Gas & Electric Company vs. Department of Taxation*, 243 Wis. 216 on page 220, the Court said:

"So far as Wisconsin's power to reach beyond its borders and to levy the tax is concerned, the United States Supreme Court has declared that Wisconsin has the right to exact the tax because of *protection given to corporate activities in this state* resulting in earnings traceable to the dividends declared and benefits to the stockholder who has received a dividend." (Italics supplied)

In its decision in *Blid vs. Wisconsin Foundry and Machinery Co.*, 243 Wis. 221, at 222, the Wisconsin Court recognizes that the corporation alone is made liable for the tax; that the corporation alone is made liable for the penalty and interest on failure to pay the tax, and that no personal liability is imposed upon the stockholder.

(4) Taxes other than special improvement taxes paid during the year upon the business or property from which the income taxed is derived, including therein taxes imposed by the state of Wisconsin and the government of the United States as income, excess or war profits and capital stock taxes, including taxes on real property which is owned and held for business purposes whether income producing or not, provided that such portion of the deduction for federal income and excess profits taxes as may be allowable shall be confined to cash payments made within the year covered by the income tax return, and provided further that deductions for income taxes paid to the United States government shall be limited to taxes paid on net income which is taxable under this chapter; and provided further that income taxes imposed by the state of Wisconsin shall accrue for the purpose of this subsection only in the year in which such taxes are assessed." (Wis. Statutes, 1935)

The determination in the case of *Wisconsin Gas & Electric Company vs. Department of Taxation*, 243 Wis. 216, was confined to the proposition that the state dividend privilege tax was not among the enumerated taxes of Section 71.03 (4) upon the payment of which a corporation was entitled to an equivalent deduction from gross income in the computation of net income for state income tax purposes. The Court said (page 219):

“The real question in this case is: On whom is the actual burden of this tax laid? This question can have but one answer. The statute specifically puts it upon the stockholder.”

The decision by this Court of the Federal question in support of the power of the state to impose the Wisconsin Privilege Dividend Tax was adopted by the Wisconsin Supreme Court with appropriate compliance and without any effort to impinge upon the declared principle. The State Court was still at liberty to determine the non-Federal question, in construing the Wisconsin State Income Tax Act, that taxes though based upon the grant of corporate privileges and for which the corporation alone is made liable were not deductible under the income tax law of the state because the ultimate economic burden was borne by the shareholder. The determination of the Wisconsin Court made no pretense of rendering a disposition of any Federal question. To import the reasoning of the Wisconsin Court into the present problem would seem to be introducing concepts of the Wisconsin system of taxation into the, otherwise, self-executing Federal Revenue structure.

The rule announced by the Wisconsin Court is not the rule in respect of taxes deductible by a corporate taxpayer under Section 23 of the Revenue Act.

Though there exist revenue provisions which require, for the purpose of certain refunds, that the taxpayer estab-

lish that he bore the economic burden of the tax as a condition of recovery (Title VII of the Revenue Act of 1936, relating to amounts collected under the Agricultural Adjustment Act), a long line of decisions establish that deduction may be made under Section 23 if the taxpayer is made liable for and pays the tax even though the economic burden may be passed on.

Prior to the time that the statute prescribed the person who might deduct estate and inheritance taxes and before the deduction of such taxes was prohibited, the United States Supreme Court held that the federal estate tax was deductible from the income of the estate as reported in the return of the executor or administrator. This notwithstanding that the ultimate burden of the tax fell upon the beneficiaries of the estate. *United States vs. Woodward*, 256 U. S. 632. Likewise, it was held that a state transfer tax imposed upon the transfer of property from a decedent and paid as required by law by the personal representative was properly deductible in the federal income tax return for the estate. In *Keith vs. Johnson*, 271 U. S. 1, the court said at page 5:

"The law plainly makes it their (the personal representatives') duty to pay the tax out of the estate. The property remaining passes to the beneficiaries. When property is transferred without the deduction of the tax the beneficiary is required to pay. But, by whomever the amount may be handed over to the state, the tax is in effect an appropriation by the state of a part of the property of the deceased at the time of death. And the state's portion is deductible from the legacy and does not pass to the legatee."

• • • • •

"While this lessens the amount for distribution among the heirs, it cannot be said that they bore any part of that tax. As well might it be claimed that they paid the funeral expenses and debts, if any, of

the intestate. No part of the transfer tax so paid could be taken by the heirs as a deduction in calculating their federal income taxes. It follows that the amount of the transfer tax paid in 1917 by the respondent was deductible in ascertaining the taxable income of the estate received by her in that year." (Page 9)

To the same effect is *United States vs. Mitchell*, 271 U. S. 9.

The opinion of the Circuit Court of Appeals, predicated upon the determination of the Wisconsin Court, for purposes solely associated with the state tax structure, of the question of the economic burden of the tax as distinguished from legal liability for the tax, seems to be at variance with the decision of this Court in *Biddle vs. Commissioner of Internal Revenue*, 302 U. S. 573. In that case, American stockholders of a British corporation in reporting United States income taxes sought the right to deduct taxes paid to the British Government in respect of dividends declared. The Circuit Court of Appeals (C. C. A. 2nd) in holding that the deduction could be taken only by the party liable for the payment of the tax without regard to its ultimate burden said:

"(A) Our system of credits and deductions is built around a concept of direct liability for taxation and direct payment. It is not administered upon the theory of ultimate burden or the final incidence of taxation. *Shearer vs. Com'r*, 48 F. (2d) 552, 555 (C. C. A. 2). In the *Shearer* case, the question was whether the purchaser of a car could deduct an excise tax which he had paid to the dealer as an item separate from the purchase price. The court, in holding that the statutory liability for the tax was upon the dealer and that therefore the deduction was properly disallowed, stated: 'If the final incidence of the burden be traced, no doubt the only income, properly speaking, which has borne the tax is the customer's, for it is a fiction to treat as income a sum received by the dealer, which, except for

the tax, would never have come to him at all. * * * But the final incidence of taxation is not a measure of the person on whom the tax is levied, and it seems to us that the form of the statute must control.'

"In other words, our system, to describe it more accurately, looks to the statutory incidence of the tax—to the party which the taxing authority has made directly responsible.

"It is admitted that under the British law the shareholder is not liable for direct assessment. He owes no direct responsibility to the taxing authority; and the corporation, a completely separate entity, pays the tax, not as the collector of revenue or as agent of the shareholder, but in discharge of a primary and sole obligation imposed upon it by the British acts. True, the shareholder may bear the ultimate burden, depending on whether the corporation declares and pays a dividend out of the profits for which it is taxed and whether, in accordance with rule 20, it elects to deduct the amount of appropriate income tax computed by the prevailing standard rate in the year of payment. Even so, he is not a taxpayer; he does not bear the statutory incidence of the tax."

Biddle vs. Commissioner, 86 Fed. (2d) 718 at 720.

In a similar case, *F. W. Woolworth Co. vs. United States*, 91 Fed. (2d) 973 (certiorari denied, 302 U. S. 768), Judge Hand, writing for the Second Circuit Court of Appeals, said:

" * * * We might agree that if the plaintiff could point to a legal duty laid upon shareholders which was discharged, section 238 (a) would protect it, but it cannot do so. At most it can say that the shareholders may in some circumstances be sureties for a tax primarily imposed upon the corporate personality, but that would not make them 'pay' the tax any more than any other surety pays when the principal pays. It does not advance the solution to say as in *United Shoe Machinery Co. vs. White*, 89 F. (2d) 363 (C. C. A. 1), that it makes no difference to the shareholder whether he pays the tax, or whether the corporation pays it and takes it out of his divi-

dend. That is true, but the final incidence of the tax does not determine its legal nature; else the shareholders would pay the normal corporate tax under our own system. We adhere to our decision in *Biddle vs. Commissioner*, supra, 86 F. (2d) 718." (Page 975)

On *certiorari* the United States Supreme Court said in *Biddle vs. Commissioner of Internal Revenue*, 302 U. S. 573:

"One of the companies availed itself of the statutory permission to declare a gross dividend, from which it deducted the tax before actual distribution, certifying to the taxpayers that the dividend would be paid 'less' income tax. The other two companies declared the dividend in the amount distributed to stockholders and certified that it was 'free of tax.' The certificates of the latter did not purport to show any deduction of tax from a gross dividend, but did indicate the amount of the tax appropriate to the dividend and showed the same net return to stockholders as if the tax had been deducted from a computed gross dividend." (Page 576)

.

"Section 131 does not say that the meaning of its words is to be determined by foreign taxing statutes and decisions, and there is nothing in its language to suggest that in allowing the credit for foreign tax payments, a shifting standard was adopted by reference to foreign characterizations and classifications of tax legislation. The phrase 'income taxes paid' as used in our own revenue laws, has for most practical purposes a well understood meaning to be derived from an examination of the statutes which provide for the laying and collection of income taxes. It is that meaning which must be attributed to it as used in Section 131.

"Hence the board's finding, supported as it is by much expert testimony, that 'the stockholder receiving the dividend is regarded in the English income tax acts as having paid "by deduction or other-

wise" the tax "appropriate" to the dividend" is not conclusive. At most it is but a factor to be considered in deciding whether the stockholder pays the tax within the meaning of our own statute. That must ultimately be determined by ascertaining from an examination of the manner in which the British tax is laid and collected what the stockholder has done in conformity to British law and whether it is the substantial equivalent of payment of the tax as those terms are used in our own statute." (Page 578)

• • • • •

"• • • The corporation pays the standard tax and against it the remedies for non-payment run." (Page 579)

• • • • •

"Although the corporation, in the United Kingdom as here, pays the tax and is bound to pay it, the tax burden in point of substance is passed on to the stockholders in the same way that it is passed on under our own taxing acts where the tax on the corporate income is charged as an expense before any part of the resulting net profit is distributed to stockholders. See Magill, Taxable Income, 24 et seq. Whether the tax is deducted from gross profits before a dividend is declared, or after, when the deduction is taken from the gross dividend, the net amount received by the stockholder is the same. Under either system, if no dividend is declared no tax is paid by the stockholder. If a dividend is declared it must be paid, however the deduction is made, from what is left after the corporation has paid taxes upon its earnings." (Page 580)

• • • • •

"Inclusion of the deducted amount in the base on which surtax is calculated, together with the provisions for refund of the tax to the stockholder who, in any event, bears its economic burden, are logical recognitions of the British conception that the stand-

ard tax paid by the corporation is passed on to the stockholders.

"Our revenue laws give no recognition to that conception. Although the tax burden of the corporation is passed on to its stockholders with substantially the same results to them as under the British system, our statutes take no account of that fact in establishing the rights and obligations of taxpayers. Until recently they have not laid a tax, except surtax, on dividends, but they have never treated the stockholder for any purpose as paying the tax collected from the corporation. Nor have they treated as taxpayers those upon whom no legal duty to pay the tax is laid. Measured by these standards our statutes afford no scope for saying that the stockholder of a British corporation pays the tax which is laid upon and collected from the corporation, and no basis for a decision that Section 131 extends to such a stockholder a credit for a tax paid by the corporation — a privilege not granted to stockholders in our own corporations. It can hardly be said that a tax paid to the Crown by a British corporation subject to United States income tax is not a tax paid within the meaning of Section 23 (c) (2) of the 1928 Act, which allows a deduction from gross income for taxes paid to a foreign country, cf. *Welch vs. St. Helens Petroleum Co.* (C. C. A. 9th), 78 F. (2d) 631, or that its stockholders could take credit under Section 131 for their share of the tax on the theory that they also had paid it." (Page 581)

In the *Biddle* case the tax which was paid by the corporation under the law of its domicile and for which it was made liable and the deduction of which could not be denied the corporation within the meaning of Section 23 (c) (2) of the 1928 Act was, nevertheless, a tax upon the income received by the shareholder. *A fortiori* a privilege dividend tax for which the corporation is made liable and which is collectible from it *only* but the validity of which rests upon

corporate privileges granted the corporation should be held deductible.

The most that can be claimed by respondent is that the State of Wisconsin in construing its own tax laws takes the British view that the deduction can be claimed only by one bearing the ultimate economic burden of the tax.

The question involved in this case is purely a federal question though it involves consideration of a tax for which the corporation is made liable by the Wisconsin Statutes. The Act is the same as that considered by this Court in *Wisconsin vs. J. C. Penney Co.*, 311 U. S. 435. The Wisconsin Court has not by any feat of construction changed or attempted to change the plain meaning of the law. Liability for the privilege tax in the present case is imposed *solely* upon the corporation with no effort made by the Wisconsin Statute to impose either a contingent or secondary liability upon the shareholder. From the standpoint of legal liability, the shareholder enters the picture only by reason of the fact that the dividends received by him bear an arithmetical relationship to the tax liability of the corporation. The instant decision of the Circuit Court of Appeals seems to have departed from the rule of law announced in the *Biddle* case.

II.

The Privilege Dividend Tax as a payment exacted from the corporation based upon the privileges extended and protection given by the state to the corporate enterprise, and measured by the exercise of a function necessary to corporate existence, is deductible if it otherwise meets the requirements of Section 23 of the Revenue Act of 1934.

Admittedly the payment by a mere volunteer of the tax liability of another does not entitle the volunteer to the deduction. Nor may one qualify for the deduction by accept-

ing and discharging a private contractual liability to pay the tax or to reimburse one liable therefore.¹

Personal liability for payment of the tax must be placed upon the person seeking the benefit of the deduction authorized. The Wisconsin Privilege Dividend Tax is sustained by both the state court and this Court as resting upon the grant by the state of corporate privileges and protection to the corporate enterprise. It is most appropriate that personal liability for payment of the tax be placed on the corporation. The imposition and measurement of the tax are related to the exercise by the corporation of a vital corporate function which conditions its very existence.

The "economic obligation" to pay dividends on stock² is essential to the survival of a corporation in the competitive effort to secure and share capital.

The payment of dividends is also necessary if profits are available therefore to avoid penalties under the Revenue Act for the unreasonable accumulation of profits.

A business privilege tax is deductible in a taxpayer's federal income tax return. (I. T. 3191, C. B. 1938-1, page 143.)

The Motor Vehicle Excise Tax under Section 900 of the Act of 1921 is deductible by the seller who is liable therefor though the burden falls upon the buyer. In respect of this tax in *Shearer vs. Commissioner*, 48 Fed. (2d) 552 (C. C. A. 2nd), the court said on page 555:

¹ *Magruder vs. Supplee*, 316 U. S. 394; *Falk Corp. vs. Commissioner*, 60 Fed. (2d) 204 (C. C. A. 7th); *Eastern Gas. & Fuel Association vs. Commissioner*, 128 Fed. (2d) 369 (C. C. A. 1st).

² See dissenting opinion of Mr. Justice Brandeis in *Missouri ex rel. S. W. Bell Tel. Co. vs. Public Service Commission*, 262 U. S. 276 at page 306.

"But the final incidence of taxation is not a measure of the person on whom the tax is levied, and it seems to us that the form of the statute must control."

Federal excise taxes on gasoline are deductible by the manufacturer, producer or importer. I. T. 3378, C. B. 1940-1, page 36, where it is said:

"The manufacturers' excise tax on gasoline imposed by section 3412 of the Internal Revenue Code is clearly imposed upon the manufacturer, producer, or importer, and is, therefore, deductible by him for Federal income tax purposes. (See Minn. 3988, C. B. XI-2 25 (1932).) The tax is not deductible from gross income in the return of the consumer even though the amount thereof is passed on to him."

Formal corporate action in the declaration of a dividend is a pre-requisite to liability for the tax. *Northwest Engineering Corp. vs. Department of Taxation*, 241 Wis. 324.¹

True, the dissenting opinion on behalf of four members of the Court written by Justice Roberts in *Wisconsin vs. J. C. Penney Co.*, 311 U. S. 435 at page 448, quoted in the opinion of trial court (R. 8) voices, as stated by the trial court, the contentions of the Government, which, if sound, invalidate the privilege dividend tax law as indicated by such dissenting opinion, but such contentions are not the law as pronounced by this Court or by the state court. Indeed, the state court whose decision voiding the Act as to dividends of foreign corporations declared outside of the state (*J. C. Penney Co. vs. Tax Commission*, 233 Wis.

¹ On page 327 the court said:

"The term 'dividend' has a well-settled meaning, and it does not extend to commercial benefits to a stockholder who buys the company's product at a discount for the purpose of dealing in that merchandise."

286) was reversed, did not use the reasoning of the dissenting opinion, but at the suit of the corporation held on the supposed authority of *Connecticut Gen. L. Ins. Co. vs. Johnson*, 303 U. S. 77, that the foreign activities of the corporation were not taxable by the state. Justice Fowler dissented. In substance his views as expressed in the dissenting opinion were vindicated by the majority decision of the Federal Supreme Court and on remand were adopted by the state court. *J. C. Penney Co. vs. Tax Commission*, 238 Wis. 69.

This Court in distinguishing the *Connecticut Gen. L. Ins. Co.* case used the following significant language:

"In the precise circumstances presented by the record it was found that the tax neither in its measure nor in its incidence was related to California transactions. Here, on the contrary, the incidence of the tax as well as its measure is tied to the earnings which the State of Wisconsin has made possible, insofar as government is the pre-requisite for the fruits of civilization for which, as Mr. Justice Holmes was fond of saying, we pay taxes." (page 446)

State of Wisconsin vs. J. C. Penney Co., 311 U. S. 435.

III.

Subsequent decisions of the Wisconsin Supreme Court have not changed the status of the Privilege Dividend Tax as it existed at the time of the trial court's decision.

True, a state court may by interpretation substantially amend or change a state statute and the statute is to be taken as so construed, but the Wisconsin Court has not by interpretation changed the plain meaning of the statute. Upon remand, the Wisconsin Court gave full exposition to the views of this Court as to the basic nature of the tax.

To adopt the views of the dissenting opinion filed in this Court would assuredly invalidate the statute.

At the time of the filing of the opinion of the trial court on September 25, 1942, the trial court had before it the decision of the state court on remand, which was rendered May 20, 1941 (*J. C. Penney Co. vs. Tax Commission*, 238 Wis. 69). The opinion of the trial court appears to be clearly sound and its validity is not disturbed by the decisions of the Wisconsin Supreme Court of June 16, 1943, in *International Harvester Co. vs. Wisconsin Department of Taxation*, 243 Wis. 198, *Wisconsin Gas & Electric Company vs. Wisconsin Department of Taxation*, 243 Wis. 216, and in *Blued vs. Wisconsin Foundry & Machine Company*, 243 Wis. 221. These decisions adhere to the decision on remand in *J. C. Penney Co. vs. Tax Commission*, 238 Wis. 69. They do not have the effect of adopting the dissenting opinion filed in this Court or introduce any new fact except the circumstance, not pertinent here, that the privilege dividend tax is not deductible for state income tax purposes by the corporate taxpayers personally liable therefor because the economic burden of the tax is passed on. There is not the slightest reason for assuming that the state court has adopted a construction of the Act which results in its invalidity. The decision of that court was directed to the question before it, namely, whether the tax paid on dividends was within the specified items of the deductibility provision of the Wisconsin income tax statute (71.03 (4)) and more specifically whether the tax was "paid during the year upon the business or property from which the income taxed is derived."

While this Court has frequently indicated the general considerations prompting it to give weight to the interpretations placed upon a state statute by the court of that state, such principle will not govern in the adjudication of fed-

eral rights. In the case of *State of New Jersey vs. Anderson*, 203 U. S. 483, at page 491, it was said:

"While we take this view of the decisions of the supreme court of New Jersey, and reach the conclusion that the claim in question is for a tax within the meaning of the law as construed by that court, the bankruptcy act is a Federal statute, the ultimate interpretation of which is in the Federal courts.

• • • • •

Conceding the doctrine that the meaning of a statute is a state question, except where rights, the subject of adjudication by the Federal courts, have accrued before its construction by the state court, or the question of contract within the protection of the Federal Constitution is involved, still a state court, while entitled to great consideration, cannot conclusively decide that to be a tax within the meaning of a Federal law providing for the payment of taxes, which is not so in fact."

Such limitation was also recognized in the case of *Carpenter vs. Shaw*, 280 U. S. 363, at page 367, where the opinion, by Justice Stone, contains this language:

"Where a Federal right is concerned we are not bound by the characterization given to a state tax by state courts or legislatures, or relieved by it from the duty of considering the real nature of the tax and its effect upon the Federal right asserted."

It is, of course, a familiar rule that the characterization or name assigned by a state court to a particular state fiscal statute is not binding upon this court. *New York, Philadelphia, & Norfolk Telegraph Co. vs. Dolan*, 265 U. S. 96, at page 98; *Stewart Dry Goods Co. vs. Lewis*, 294 U. S. 550, at page 555. In *Schuylkill Trust Co. vs. Pennsylvania*, 296 U. S. 113, at page 119, it was said in the opinion rendered by Justice Roberts:

"We give great weight to the characterization of a tax, or the interpretation of a state law, emanating

from the highest court of the state, but where a federal question is involved we are not bound by the label attached to the tax or the character ascribed to the law. We must determine for ourselves the true nature of the tax by ascertaining its operation and effect."

In the brief filed below on behalf of the Government, reliance was therein placed upon the case of *National Bank of Commerce vs. Allen*, 223 Fed. 472 (C. C. A. 8th). It is submitted that there is nothing in such case which aids the Government's position. There the State Personal Property Tax was specifically exerted against the shares of stock held by the stockholders of the bank. The State was without power to tax the bank as such. The statute was construed so as to sustain its validity and was held to be a tax upon the shareholders and not upon the bank. The property taxed did not belong to the bank but to the shareholders.

The case of *Central Bank vs. United States*, 137 U. S. 355, also cited by the Government in its brief below, seems to be clearly lacking in pertinency. The tax there was not upon a corporate privilege and did not involve the passing on of the economic burden of the tax. The court declared (page 363):

"The tax is constituted a claim against the stockholders only and the bank was made simply an agent to collect them for the state."

IV.

Regulations as between corporation and shareholder imposed by the State of Wisconsin in the exercise of its power over corporations domiciled in the state or foreign corporations licensed therein have no more effect on the status of the tax payment under federal law than a contractual arrangement for the sharing of the tax burden.

The State of Wisconsin under its reserved power in respect of the corporate charters (Section 1 of Article XI of the Wisconsin Constitution) may regulate the internal affairs of Wisconsin corporations. All shareholders hold their stock subject to the exercise of such legislative power. *Vieux vs. Sixth Ward Building & Loan Association*, 310 U. S. 32; *Schuylkill Trust Co. vs. Pennsylvania*, 302 U. S. 506, 514; see also *State Tax Comm. of Utah vs. Aldrich*, 316 U. S. 174-181. In the case of *Rogers vs. Guaranty Trust Co.*, 288 U. S. 123, such view was expressed at Page 130 in the following language:

“When, by acquisition of his stock, plaintiff became a member of the corporation he, like every other shareholder, impliedly agreed that in respect of its internal affairs the company was to be governed by the laws of the State in which it was organized.”

In respect of foreign corporations, the state generally has a broad power to compel their submission to regulations imposed upon corporations of the domicile.

Provisions of the privilege dividend tax law, which pass on the economic burden of the tax considered as in effect an amendment of the corporate charter, became contractual as between the corporation and the shareholder just as the trust indenture of the corporation in *Eastern Gas & Fuel Association vs. Commissioner*, 128 Fed. (2d) 369 (C. C. A. 1st) assumed contractually to pay the state income taxes of shareholders where the corporation creating the trust

indenture was under no obligation to pay such taxes. However, the analogy of contractual relationship applies only to the factor of the economic burden of the tax since the duty of the corporation to pay the tax is clearly of statutory rather than of contractual origin.

As the economic burden of all corporate taxes falls upon the shareholders, the direction of the Wisconsin Statute that the amount of the tax be deducted from the dividend reaches only a matter of empty form.

If the corporation proposes to distribute one dollar per share to its common stockholders, literal observance of the statute would require that the distribution in form be \$1.00 per share plus the tax, that the tax after being so added be then subtracted and the \$1.00 remitted. If, however, the corporation announces that it will pay the tax and declares a tax-free net dividend of one dollar per share, the result is the same. In each instance the state will receive the same amount of tax, the common stockholder will receive the same amount upon his share holdings, and the corporate cash and undistributed surplus accounts will be exactly the same.

If a corporation were to declare and pay a net common dividend without including the amount of the tax therein but paying the proper tax to the state and announcing its purpose in that respect, it seems clear that no court would recognize that any party was aggrieved by the form of the procedure or attempt, by mandamus or otherwise, to compel the corporation to make the idle gesture contemplated by statute. This is exactly in accord with the order of the Wisconsin Tax Commission promulgated March 4, 1938. (Prentice-Hall, State and Local Tax Service—Wisconsin, Section 13,288.) (Footnote, page 10)

When the corporation pays the tax, corporate assets are depleted by the amount of the payment. There is no true

reimbursement by the shareholder. The depletion is not restored. It is to be noted that the privilege dividend tax is computed on the amount of dividend *paid*, not on the amount of dividend including tax declared. The state legislature in putting the economic burden of the tax on the shareholder has merely recognized the inevitable. The burden could not fall elsewhere.

V.

If, notwithstanding the decisions of the Wisconsin Supreme Court and the Federal Supreme Court holding the Privilege Dividend Tax to be incident to corporate privileges and protection extended by the state it is held that the tax is imposed upon the shareholder, it is still deductible under Section 23(d) of the Revenue Act of 1934.

Petitioner in Section V of its brief filed with the Circuit Court of Appeals asserted, as an alternative contention, that if it should be held that the Wisconsin Privilege Tax was imposed upon the shareholder it is, nevertheless, deductible under Section 23 (d) of the Revenue Act of 1934. The opinion of that Court makes no reference to such assertion. The mandate, however, is one of complete reversal of the judgment of the Trial Court. It would appear that such proposition has never before received the attention of this Court.

Petitioner has heretofore endeavored to point out cogent reasons for regarding the tax involved herein as one imposed upon the corporation. If, however, it is determined that the tax is imposed upon the shareholder, its deductibility is claimed under Section 23 (d) of the Revenue Act of 1934 which admits of deduction "in case of taxes imposed upon a shareholder of a corporation upon his interest as shareholder which are paid by the corporation without reimbursement from the shareholder * * *".

In *Eastern Gas & Fuel Association vs. Commissioner*, 128 Fed. (2d) 369 (C. C. A. 1st), it was held that this provision relates only to taxes upon shares of property represented by shares and not to taxes on the income of the shares or receipt of part of the property represented by the shares. In view of the legislative history of the Act, we doubt the soundness of this conclusion. Section 23 (d) was first introduced as a part of the Revenue Act of 1921. The Conference Committee report agreeing to a Senate change states:

"This amendment provides that a tax of the kind generally allowed as a deduction may be taken as a deduction by a corporation if it is a tax imposed upon a shareholder or member upon his interest as such and paid by the corporation without reimbursement from the shareholder, further providing that in such case no deduction shall be allowed the shareholder," (1939-1 C. B. (Part 2) 221)

The expression "interest as a shareholder" would seem to include all of the rights inuring to a person by virtue of his holding stock. The right to dividends is an incident to the ownership of stock. In *re Starbuck's Executrix*, 251 N. Y. 439. The *Restatement of the Law, Conflict of Laws*, in Section 42 (b) defines interest to include "varying aggregates of rights, privileges, powers and immunities and distributively to mean any one of them."

The words "interest in property" have been used for many years in the Federal Estate Tax Law as embracing all types of property rights, including many rights amounting to less than a fee.

One who has the right to the income from property for life clearly has an "interest therein." In the case of a transfer of stock with the income to one for life and remainder to another, it would seem quite clear that both life tenant and remainderman have an interest as a shareholder. The interest of the former is the right to receive the divi-

dends, and a tax upon that right is a tax upon his interest in the corporation within the meaning of Section 23 (d). Thus, a tax upon the right to receive dividends, if paid by the corporation without reimbursement, appears to meet every test of deductibility under subsection (d) of Section 23 of the Revenue Act of 1934.

Payment by petitioner as a corporation is admitted. If the tax is imposed upon a shareholder, it would seem to be "upon his interest as shareholder." Such expression would appear to include all of the rights inuring to a person by virtue of his holding stock including the right to dividends as an incident to the ownership thereof. The word "interest" is one of extremely broad import and it cannot be presumed that Congress intended its use in any narrow or restricted sense.

There has been no reimbursement to the corporation from the shareholder and the theory of the economic incidence of the tax cannot reasonably be indulged in or used as a legal fiction to supply the element of reimbursement. The question of the economic incidence of a tax as between a shareholder and a corporation was discussed in the case of *Biddle vs. Commissioner of Internal Revenue*, 302 U. S. 573, and the following language was used at p. 580:

"Although the corporation, in the United Kingdom as here, pays the tax and is bound to pay it, the tax burden in point of substance is passed on to the stockholders in the same way that it is passed on under our own taxing acts where the tax on the corporate income is charged as an expense before any part of the resulting net profit is distributed to stockholders. See Magill, *Taxable Income*, 24 et seq. Whether the tax is deducted from gross profits before a dividend is declared, or after, when the deduction is taken from the gross dividend, the net amount received by the stockholder is the same. Under either system, if no dividend is declared no tax is paid by the stockholder. If a dividend is declared it must

be paid, however the deduction is made, from what is left after the corporation has paid taxes upon its earnings * * * " (page 580)

Reimbursement clearly connotes action of repayment made after an initial payment. *Webster's New International Dictionary* defines the word reimburse as meaning "to pay back; repay * * * to make restoration or payment of an equivalent to (a person)". The elements of deductibility under subsection (d) of Section 23 of the Revenue Act of 1934 seem to exist and if the tax presently involved is regarded as one imposed upon a shareholder it is, nevertheless, deductible by the corporation.

CONCLUSION.

This Court found it necessary to deny the correctness of the state court's conclusion in *J. C. Penney Co. vs. Tax Commission*, 233 Wis. 286, that the tax as applied to the dividends of a foreign corporation declared outside of the state is violative of the Federal Constitution because the privilege of declaring such dividends was not granted by the state of Wisconsin. It is not fair to assume that the Wisconsin Court refused to accept either the letter or substance of such determination of this Court, despite any divergence in nomenclature which may still persist between the two jurisdictions. Both Courts are now agreed that the tax rests upon corporate privileges and protection granted by the state of Wisconsin and is collectible on dividends declared by a foreign corporation outside of the state to the extent that income earned in Wisconsin is distributed and that the tax is a charge for the grant of corporate privileges. The obligation to pay such a tax should and does rest primarily on the direct beneficiary of such corporate privileges. The corporation itself is the

direct beneficiary of the state indulgence in return for which the tax is imposed.

A corporation does not occupy the position of a mere collector of a tax nor act either as agent for the state or for the shareholder when only the corporation is personally liable therefor and the tax itself is a charge based upon the enjoyment by it of corporate protection and privileges extended by the state. This is not changed by the legislative direction that as a matter of internal arrangement between the corporation and its shareholders the latter are to bear the ultimate burden of the tax as they inevitably bear the burden of all corporate taxes.

The judgment of the United States Circuit Court of Appeals for the Seventh Circuit should be reversed.

Respectfully submitted,

VAN B. WAKE,
Attorney for Petitioner.

773 North Broadway,
Milwaukee (2) Wisconsin.

February, 1944.



APPENDIX.

Wisconsin Privilege Dividend Tax.

Laws of Wisconsin (1935), c. 505, Sec. 3, as amended by Laws of Wisconsin (1935), c. 552, Sec. 1.

Section 3. *Privilege dividend tax.* (1) For the privilege of declaring and receiving dividends, out of income derived from property located and business transacted in this state, there is hereby imposed a tax equal to two and one-half per centum of the amount of such dividends declared and paid by all corporations (foreign and local), except those specified in paragraphs (d) and (g) of Section (1) of Section 71.05 of the Statutes, after the passage and publication of this act and prior to July 1, 1937. Such tax shall be deducted and withheld from such dividends payable to residents and non-residents by the payor corporation.

(2) Every corporation required to deduct and withhold any tax under this section shall, on or before the last day of the month following the payment of the dividend, make returns thereof and pay the tax to the tax commission, reporting such tax on the forms to be prescribed by the tax commission.

(3) Every such corporation hereby made liable for such tax, shall deduct the amount of such tax from the dividends so declared.

(4) In the case of corporations doing business within or without the state of Wisconsin, such tax shall apply only to dividends declared and paid out of income derived from business transacted and property located within the state of Wisconsin. The amount of income attributable to

this state shall be computed in accordance with the provisions of chapter 71. In the absence of proof to the contrary, such dividends shall be presumed to have been paid out of earnings of such corporation attributable to Wisconsin under the provisions of chapter 71, for the year immediately preceding the payment of such dividend. If a corporation had a loss for the year prior to the payment of the dividend, the tax commission shall, upon application, determine the portion of such dividend paid out of corporate surplus and undivided profits derived from business transacted and property located within the state.

(5) Dividends paid by a subsidiary corporation to its parent shall not be subject to the tax herein imposed provided that the subsidiary and its parent report their income for taxation under the provisions of chapter 71 on a consolidated income return basis, or both corporations report separately.

(6) The provisions of this section shall not apply to dividends declared and paid by a Wisconsin corporation out of its income which it has reported for taxation under the provisions of chapter 71, if the business of such corporation consists in the receipt of dividends and the distribution thereof to its stockholders.

(7) For the purposes of this section dividends shall be defined as in section 71.02, except that the tax herein imposed shall not apply to stock dividend or liquidating dividends.

(8) The tax hereby levied, if not paid within the time herein provided, shall become delinquent and when delinquent shall be subject to a penalty of two per cent on the amount of the tax and interest at the rate of one-half per cent per month until paid.

(9) The tax hereby imposed shall, when collected by the tax commission, be paid by it into the state treasury.

Extract from the Revenue Act of 1934.

"Sec. 23. Deductions from gross income.

In computing net income there shall be allowed as deductions:

(a) Expenses. . . .

(b) Interest. . . .

(c) Taxes Generally. Taxes paid or accrued within the taxable year, except—

(1) Federal income, war-profits, and excess-profits taxes;

(2) income, war-profits, and excess-profits taxes imposed by the authority of any foreign country or possession of the United States; but this deduction shall be allowed in the case of a taxpayer who does not signify in his return his desire to have to any extent the benefits of section 131 (relating to credit for taxes of foreign countries and possessions of the United States);

(3) estate, inheritance, legacy, succession, and gift taxes; and

(4) taxes assessed against local benefits of a kind tending to increase the value of the property assessed; but this paragraph shall not exclude the allowance as a deduction of so much of such taxes as is properly allocable to maintenance or interest charges.

(d) *Taxes of shareholder paid by corporation.* — The deduction for taxes allowed by subsection (c) shall be allowed to a corporation in the case of taxes imposed upon a shareholder of the corporation upon his interest as shareholder which are paid by the corporation without reimbursement from the shareholder, but in such cases no deduction shall be allowed the shareholder for the amount of such taxes."

INDEX

| | Page |
|--|------|
| Opinions below..... | 1 |
| Jurisdiction..... | 1 |
| Question presented..... | 2 |
| Statutes and regulations involved..... | 2 |
| Statement..... | 6 |
| Argument..... | 8 |
| Conclusion..... | 15 |

CITATIONS

Cases:

| | |
|--|----------|
| <i>Biddle v. Commissioner of Internal Revenue</i> , 302 U. S. 573..... | 11 |
| <i>Blid v. Wisconsin Foundry and Machine Co.</i> , 243 Wis. 221, 10 N. W. (2d) 142..... | 14 |
| <i>Eastern Gas & Fuel A. v. Commissioner</i> , 128 F. 2d 369..... | 13 |
| <i>Eliot Nat. Bank v. Gill</i> , 218 Fed. 600..... | 13 |
| <i>Ferguson v. Fidelity Union Trust Co.</i> , 24 F. 2d 520..... | 13 |
| <i>First Nat. Bank of Jackson, Miss. v. McNeel</i> , 238 Fed. 559..... | 13 |
| <i>Keith v. Johnson</i> , 271 U. S. 1..... | 10, 11 |
| <i>Magruder v. Supplee</i> , 316 U. S. 394..... | 10, 11 |
| <i>Natl. Bank of Commerce v. Allen</i> , 223 Fed. 472..... | 13 |
| <i>Northern Trust Co. v. McCoach</i> , 215 Fed. 991..... | 13 |
| <i>Porter v. United States</i> , 27 F. 2d 882..... | 13 |
| <i>United States v. Guaranty Trust & Savings Bank</i> , 253 Fed. 291..... | 13 |
| <i>Wisconsin v. J. C. Penney Co.</i> , 311 U. S. 435..... | 8, 9, 10 |
| <i>Wisconsin Gas & Electric Co. v. Wisconsin Department of Taxation</i> , 243 Wis. 216, 10 N. W. (2d) 140..... | 10 |

Statutes:

| | |
|---|---------------|
| Revenue Act of 1921, c. 136, 42 Stat. 227: | |
| Sec. 214..... | 13 |
| Sec. 234..... | 13 |
| Revenue Act of 1928, Sec. 131(a)(1)..... | 11 |
| Revenue Act of 1934, c. 277, 48 Stat. 680, Sec. 23.... | 2, 12, 13, 14 |
| Laws of Wisconsin (1935), c. 505, Sec. 3, as amended by Laws of Wisconsin (1935), c. 552, Sec. 1, and Laws of Wisconsin (1937), c. 233, Sec. 1..... | 3-6 |

Miscellaneous:

| | |
|--|----|
| I. T. 3002, XV-2 Cum. Bull. 142 (1936)..... | 6 |
| S. Rep. No. 275, 67th Cong., 1st Sess., p. 19..... | 13 |
| Treasury Regulations 86: | |
| Art. 23(c)-1..... | 3 |
| Art. 23(d)-1..... | 3 |



In the Supreme Court of the United States

OCTOBER TERM, 1943

No. 565

WISCONSIN GAS & ELECTRIC COMPANY, PETITIONER

v.

THE UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED
STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH
CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The opinion of the district court (R. 6-8) is reported in 46 F. Supp. 929. The opinion of the circuit court of appeals (R. 20-23) is reported in 138 F. (2d) 597.

JURISDICTION

Judgment of the circuit court of appeals was entered on November 8, 1943 (R. 23). The petition for writ of certiorari was filed on December 30, 1943. The jurisdiction of this Court is

invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the Wisconsin Gas and Electric Company, in computing its net income for the year 1935, is entitled under Section 23 (c) or (d) of the Revenue Act of 1934 to a deduction for amounts paid to the State of Wisconsin pursuant to the privilege dividend tax law of that state.

STATUTES AND REGULATIONS INVOLVED

Revenue Act of 1934, c. 277, 48 Stat. 680:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions;

* * * *

(c) *Taxes Generally.*—Taxes paid or accrued within the taxable year, except—[exceptions not material].

* * * *

(d) *Taxes of Shareholder Paid by Corporation.*—The deduction for taxes allowed by subsection (c) shall be allowed to a corporation in the case of taxes imposed upon a shareholder of the corporation upon his interest as shareholder which are paid by the corporation without reimbursement from the shareholder, but in such cases no deduction shall be allowed the shareholder for the amount of such taxes.

* * * *

Treasury Regulations 86, promulgated under the Revenue Act of 1934:

ART. 23 (c)-1. *Taxes*.—Subject to the exceptions stated in this article and articles 23 (c)-2 and 23 (c)-3, * * * [exceptions not material] taxes imposed by * * * any State or Territory * * * are deductible from gross income for the year in which paid or accrued * * *. In general taxes are deductible only by the person upon whom they are imposed. * * *

ART. 23 (d). *Tax on bank or other stock*.—Banks or other corporations paying taxes assessed against their shareholders on account of their ownership of the shares of stock issued by such corporations without reimbursement from such shareholders may deduct the amount of taxes so paid. The Act specifically provides, however, that in such cases the shareholders may not deduct the amount of the taxes. The amount so paid should not be included in the income of the shareholder.

* * * * *

Laws of Wisconsin (1935), c. 505, Sec. 3, as amended by Laws of Wisconsin (1935), c. 552, Sec. 1, and Laws of Wisconsin (1937), c. 233, Sec. 1:

SECTION 3. PRIVILEGE DIVIDEND TAX. (1)

For the privilege of declaring and receiving dividends, out of income derived from property located and business transacted in this state, there is hereby imposed a tax equal to two and one-half per centum of

the amount of such dividends declared and paid by all corporations (foreign and local), *except those specified in paragraphs (d) and (g) of Section (1) of Section 71.05 of the Statutes,*¹ after the passage and publication of this act and prior to July 1, 1937. Such tax shall be deducted and withheld from such dividends payable to residents and nonresidents by the payor corporation.

(2) Every corporation required to deduct and withhold any tax under this section shall, on or before the last day of the month following the payment of the dividend, make return thereof and pay the tax to the tax commission, reporting such tax on the forms to be prescribed by the tax commission.

(3) Every such corporation hereby made liable for such tax, shall deduct the amount of such tax from the dividends so declared.

(4) In the case of corporations doing business within and without the state of Wisconsin, such tax shall apply only to dividends declared and paid out of income derived from business transacted and property located within the state of Wisconsin. The amount of income attributable to this state shall be computed in accordance with the provisions of chap-

¹ The clause in italics was inserted by Laws of Wisconsin (1937), c. 233, Sec. 1. Section 4 of that chapter gives this amendment retroactive and prospective effect. Sections 71.05 (1) (d) and (g), Wisconsin Statutes, contain the exemption provisions of the Wisconsin income-tax law.

ter 71. In the absence of proof to the contrary, such dividends shall be presumed to have been paid out of earnings of such corporation attributable to Wisconsin under the provisions of chapter 71, for the year immediately preceding the payment of such dividend. If a corporation had a loss for the year prior to the payment of the dividend, the tax commission shall upon application, determine the portion of such dividend paid out of corporate surplus and undivided profits derived from business transacted and property located within the state.

(5) Dividends paid by a subsidiary corporation to its parent shall not be subject to the tax herein imposed provided that the subsidiary and its parent report their income for taxation under the provisions of chapter 71 on a consolidated income return basis, or both corporations report separately.

(6) The provisions of this section shall not apply to dividends declared and paid by a Wisconsin corporation out of its income which it has reported for taxation under the provisions of chapter 71, to the extent that the business of such corporation consists in the receipts of dividends from which a privilege dividend tax has been deducted and withheld and the distribution thereof to its stockholders.

(7) For the purposes of this section dividends shall be defined as in section 71.02, except that the tax herein imposed shall

not apply to stock dividend or liquidating dividends.

(8) The tax hereby levied, if not paid within the time herein provided, shall become delinquent and when delinquent shall be subject to a penalty of two per cent on the amount of the tax and interest at the rate of one-half per cent per month until paid.

(9) The tax hereby imposed shall, when collected by the tax commission, be paid by it into the state treasury.

* * * * *

STATEMENT

The petitioner is a Wisconsin corporation doing business wholly within that State as a utility company (R. 5).

On its final income tax return for the calendar year 1935, petitioner claimed a deduction from gross income of \$3,750 for payment of the Wisconsin privilege dividend tax (R. 5).

Following an audit by a revenue agent, a deficiency assessment of additional tax in the amount of \$11,696 was made with respect to petitioner's income for 1935 (R. 5). This deficiency assessment was predicated in part on the disallowance of the deduction for the dividend tax² (R. 6).

² Disallowance of this deduction was pursuant to I. T. 3002, XV-2 Cum. Bull. 142 (1936), which provides:

"Advice is requested whether, for Federal income tax purposes, the corporation paying a dividend or the stockholder

To this deficiency assessment was added interest in the amount of \$847.56,³ bringing the total to \$12,543.56 (R. 5). Of this amount, \$12,504.30 was paid by petitioner on May 10, 1937, and on October 26, 1937, the remainder of the assessment, namely, \$39.26, was abated (R. 6).

On May 9, 1939, petitioner timely filed with the Collector of Internal Revenue a claim for refund of tax paid with respect to income of 1935, one ground of which was petitioner's claim for deduction of dividend tax ~~paid~~ in that year. This claim for refund to the extent based upon the deduction for dividend tax was denied by the

receiving it is entitled to deduct the privilege dividend tax of 2½ per cent imposed by the State of Wisconsin under section 3 of chapter 505, Laws of Wisconsin, 1935.

* * * * *

"The title of the law and its provisions show that it was the intention of the State legislature to levy an excise tax on the receipt of dividends and to make the corporation declaring and paying the dividend the collector of the tax for and on behalf of the State by requiring the corporation to withhold the tax from the stockholder and to pay the amount withheld to the State tax commission, which in turn pays it into the State treasury.

* * * * *

"It is held that the privilege dividend tax is an excise tax imposed upon the stockholder receiving the dividend, who may deduct the amount of the tax in his Federal income tax return. The stockholder, however, should report in his return the full amount of the dividend, including the tax withheld."

³ In paragraph 5, stipulation for agreed statement of facts (R. 5), the amount of interest was erroneously stated to be \$847.96. The difference is immaterial here.

Commissioner of Internal Revenue on October 31, 1940 (R. 6). The present action for recovery of refund on this ground was commenced on February 19, 1941 (R. 3).

The district court filed its opinion in this case on September 25, 1942 (R. 6-8), to the effect that petitioner was entitled to a deduction for the dividend tax here involved. This conclusion was predicated by the district court entirely upon the decision of this Court in *Wisconsin v. J. C. Penney Co.*, 311 U. S. 435. Pursuant to this opinion judgment by the district court was filed on October 6, 1942 (R. 10-11).

On appeal to the United States Circuit Court of Appeals for the Seventh Circuit that court on November 8, 1943, rendered a decision holding that taxpayer was not entitled to the deduction for dividend tax (R. 20-23). The judgment of the district court was reversed (R. 23).

ARGUMENT

1. In support of its petition for a writ of certiorari the petitioner asserts that the decision below conflicts with the decision of this Court in *Wisconsin v. J. C. Penney Co.*, 311 U. S. 435. We submit that no such conflict exists.

In the *Penney* case this Court had before it the constitutional validity of the Wisconsin dividend tax statute as applied to a Delaware corporation, with its principal offices in New York,

but doing business in the State of Wisconsin and other states, and having stockholders in the State of Wisconsin and other states. The decision upheld the validity of the dividend tax as against claims of violation of the Fourteenth Amendment to the Constitution of the United States. While it is true that, in the course of its analysis of the "practical operation" of the dividend tax, this Court in the *Penney* case likened the tax to "an additional tax on corporate earnings within Wisconsin" (p. 442), the opinion does not appear to contain, either expressly or by necessary implication, any holding that the tax is one imposed on the corporation itself, as distinguished from its stockholders. Rather, the Court appears to have concerned itself primarily with the question "whether the taxing power exerted by the state bears fiscal relation to protection, opportunities and benefits given by the state," or, as alternatively stated in the opinion, "whether the state has given anything for which it can ask return" (p. 444). This question the Court answered in the affirmative, holding that "the substantial privilege of carrying on business in Wisconsin, which has here been given, clearly supports the tax" (pp. 444-445).

The *Penney* case thus established the constitutional validity of the dividend tax as applied to foreign corporations. There being no question here presented as to the constitutionality of the

dividend tax,⁴ the only question before the court below was whether this tax, already held in the *Penney* case to be a constitutional exaction, was imposed on the petitioner or on its stockholders. This question, which was not decided or involved in the *Penney* case,⁵ depends in turn for its answer upon Wisconsin law (*Keith v. Johnson*, 271 U. S. 1, 8; *Magruder v. Supplee*, 316 U. S. 394, 396), and since the decision of the district court herein it has been unequivocally answered by the Supreme Court of Wisconsin contrary to the contentions of the petitioner. *Wisconsin Gas & Electric Co. v. Wisconsin Department of Taxation*, 243 Wis. 216, 10 N. W. (2d) 140 (1943); *Blid v. Wisconsin Foundry & Machine Co.*, 243 Wis. 221, 10 N. W. (2d) 142 (1943). These decisions of the Wisconsin Supreme Court, holding that the tax is imposed on the stockholders rather than the corporation, were concededly followed by the court below, and its action in following them is in accord with applicable decisions of this Court, and presents no question requiring review by this Court.

⁴The petitioner is a Wisconsin corporation, and is not shown even to have foreign stockholders (R. 23). As the court below said (R. 23): "Power to tax was the only question before the court in the *Penney* case. Who shall be entitled to enjoy some incidence of the tax payment is our question. * * * the factual situation is clearly distinguishable from the *Penney* case."

⁵There was no suggestion in the *Penney* case that the benefits flowing from "the substantial privilege of doing business in Wisconsin" must be entirely absorbed by the cor-

2. Nor does the decision below present any conflict with the decision of this Court in *Biddle v. Commissioner of Internal Revenue*, 302 U. S. 573. There this Court, in the apparent absence of controlling English decisions, considered and construed the British tax law, and held that American taxpayers who had received dividends on their stock in British corporations were not entitled under Section 131 (a) (1) of the Revenue Act of 1928 to a credit for "income * * * taxes paid or accrued during the taxable year to [a] foreign country," measured by their respective proportions of the tax paid by the British corporations to the British Government on the profits out of which the dividends were declared. Passing differences between the British income tax law and the Wisconsin dividend tax law, it is apparent that here the Wisconsin Supreme Court has explicitly construed the dividend tax law on the precise point at issue. Under the settled doctrine of this Court, that construction should under the circumstances presented here be accepted by the federal courts. *Keith v. Johnson*, 271 U. S. 1, 8; *Magruder v. Supplee*, 316 U. S. 394, 396.

In the *Biddle* case this Court held that the application of the term "income taxes paid" as used in the Revenue Act of 1928 was not to be de-

poration in order to sustain the constitutionality of the tax. A postulate of the case was that the benefits, at least to a degree, flowed on to the stockholders and were enjoyed by them in the form of dividends out of corporate earnings.

terminated by any "shifting standard . . . adopted by reference to foreign characterizations and classifications of tax legislation," but rather by "an examination of the statutes which provide for the laying and collection of income taxes" in order to determine "what the stockholder has done . . . and whether it is the substantial equivalent of payment of the tax as those terms are used in our own statute" (p. 579). We take this to mean no more than that in the absence of clear determination by the local courts as to the actual incidence of a state or foreign tax, the federal courts are to examine the question for themselves, accepting available "foreign characterizations and classifications" not as controlling authority, but as "a factor to be considered in deciding whether the stockholder pays the tax." Here, the Wisconsin Supreme Court has determined that the actual incidence of the dividend tax is on the stockholder, and not on the corporation—that is, that the stockholder pays the tax. Under the rule of the cases cited the determination of that court should under the circumstances here presented be regarded as conclusive of the issue.

3. The petitioner contends, as an alternative ground for recovery, that it is in any event entitled to the deduction permitted by Section 23 (d) of the Revenue Act of 1934 for "taxes imposed upon a shareholder of the corporation upon his interest as shareholder which are paid

by the corporation without reimbursement from the shareholder.”*

This contention rests on an assumption that the tax, if regarded as imposed on the stockholder rather than the corporation, is imposed “upon his interest as shareholder.” This assumption is refuted by the legislative history of Section 23 (d) and has no support in judicial decisions. In *Eastern Gas and Fuel A. v. Commissioner*, 128 F. (2d) 369 (C. C. A. 1, 1942), it was held that “the use of the term ‘interest’ relates to a tax upon the ownership of stock and not to the income derived therefrom,” and that therefore

* This contention was likewise pressed before the court below, although not considered by that court in its opinion.

Section 23 (d) was derived from Sections 214 (a) (3) (d) and 234 (a) (3) of the Revenue Act of 1921. These provisions in turn had been adopted to resolve a controversy which had given rise to considerable litigation, under earlier revenue acts, as to the proper person entitled to deduction for state intangible personal property taxes, imposed largely upon bank stock. Cf. *Porter v. United States*, 27 F. (2d) 882 (C. C. A. 9, 1923), *First Nat. Bank of Jackson, Miss. v. McNeel*, 238 Fed. 559 (C. C. A. 5, 1917), *Natl. Bank of Commerce v. Allen*, 223 Fed. 472 (C. C. A. 8, 1915), *Eliot Nat. Bank v. Gill*, 218 Fed. 600 (C. C. A. 1, 1914), and *Northern Trust Co. v. McCoach*, 215 Fed. 991 (E. D. Pa., 1914), in all of which it had been held that the state intangible personal property tax was imposed upon the stockholder and deductible only by him; contra, *Ferguson v. Fidelity Union Trust Co.*, 24 F. (2d) 520 (C. C. A. 3, 1928); *United States v. Guaranty Trust & Savings Bank*, 253 Fed. 291 (S. D. Fla., 1918). The limited purpose of the provision in the Revenue Act of 1921 is shown by the report on the bill by the Senate Committee on Finance (S. Rep. No. 275, 67th Cong., 1st sess., p. 19).

Section 23 (d) did not permit a deduction to a Massachusetts trust for state income taxes paid by it with respect to dividends paid to its preferred stockholders. We are aware of no conflicting cases, and the petitioner cites none. At no point in the extensive litigation relating to the Wisconsin dividend tax law has there been any suggestion that the tax in any way resembles an *ad valorem* tax imposed upon a property interest.

Furthermore, as shown above, the Wisconsin Supreme Court has held that, although as a convenient mechanical device the tax is collected from the corporation, the incidence of the tax is not upon the corporation but upon the stockholder. The holding of that court in *Blid v. Wisconsin Foundry & Machine Co.*, 243 Wis. 221, 10 N. W. (2d) 142 (1943), was that the stockholder cannot recover from the corporation his proportion of the dividend tax paid because the tax is imposed upon him and not upon the corporation. This holding carries with it the corollary that even if the corporation is regarded as paying the tax in the first instance it is entitled to reimbursement out of funds belonging to the stockholder. A corporation so entitled to reimbursement does not fall within the class of taxpayers entitled to deduction under Section 23 (d).

We submit, therefore, that this argument is without merit, and that in any event it presents

no conflict of decisions nor any other ground for review by this Court.

CONCLUSION

For the foregoing reasons the petition for a writ of certiorari should be denied.

Respectfully submitted.

CHARLES FAHY,
Solicitor General.

SAMUEL O. CLARK, Jr.,
Assistant Attorney General.

SEWALL KEY,
CHESTER T. LANE,
T. CARROLL SIZER,

Special Assistants to the Attorney General.

JANUARY 1944.

INDEX

| | |
|--|-----------|
| Opinions below..... | Page 1 |
| Jurisdiction..... | 1 |
| Question presented..... | 2 |
| Statutes and regulations involved..... | 2 |
| Statement..... | 2 |
| Summary of argument..... | 3 |
| Argument: | |
| I. The Wisconsin privilege dividend tax is not imposed upon the corporation but upon the shareholders, and is therefore not a tax deductible by the corporation under the provisions of Section 23 (c) of the Revenue Act..... | 6 |
| 1. Taxes are deductible only by the person upon whom they are imposed..... | 7 |
| 2. Whether a particular state tax is imposed upon the taxpayer claiming its deduction is determined by the decisions of the courts of the state which levied the tax..... | 9 |
| 3. The Wisconsin privilege dividend tax by its express terms, and as construed by the Wisconsin Supreme Court, is imposed upon the shareholders of the corporation and not upon the corporation itself..... | 12 |
| 4. The decisions of this Court in <i>Wisconsin v. J. C. Penney Co.</i> and <i>Biddle v. Commissioner</i> are not applicable to the present case..... | 23 |
| II. The taxpayer is not entitled under Section 23 (d) of the Revenue Act of 1934 to a deduction of the Wisconsin privilege dividend tax..... | 31 |
| Conclusion..... | 37 |
| Appendix A..... | 38 |
| Appendix B..... | 43 |

CITATIONS

| | |
|--|----------------------|
| Cases: | |
| <i>Alabama v. King & Boozer</i> , 314 U. S. 1..... | 12 |
| <i>Allen v. Regents of the University System of Georgia</i> , 304 U. S. 439..... | 15 |
| <i>American National Bank of St. Paul v. Commissioner</i> , 14 B. T. A. 476..... | 12, 16, 33 |
| <i>Biddle v. Commissioner</i> , 302 U. S. 573..... | 5, 6, 27, 28, 29, 30 |
| <i>Blief v. Wisconsin Foundry & Machine Co.</i> , 243 Wis. 221.. | 17, 18 |

Cases—Continued.

| | Page |
|---|-------------------|
| <i>Cohan v. Commissioner</i> , 11 B. T. A. 743..... | 9 |
| <i>Colorado Bank v. Bedford</i> , 310 U. S. 41..... | 21, 30 |
| <i>Commissioner v. Coward</i> , 110 F. 2d 725..... | 9, 12, 30 |
| <i>Commissioner v. Heininger</i> , No. 63, present Term, decided December 20, 1943..... | 26 |
| <i>Commissioner v. Plestcheeff</i> , 100 F. 2d 62..... | 9, 12 |
| <i>Commissioner v. Rust's Estate</i> , 116 F. 2d 636..... | 12 |
| <i>Corry v. Baltimore</i> , 196 U. S. 466..... | 27 |
| <i>Curry v. McCanless</i> , 307 U. S. 357..... | 24 |
| <i>Eastern Gas & Fuel A. v. Commissioner</i> , 128 F. 2d 369..... | 9, 35 |
| <i>Eckstein v. Commissioner</i> , 41 B. T. A. 746..... | 9, 12 |
| <i>Eisenberg v. Commissioner</i> , 11 B. T. A. 574..... | 9 |
| <i>Eliot Nat. Bank v. Gill</i> , 218 Fed. 600..... | 8, 15, 33 |
| <i>Falk Corp. v. Commissioner</i> , 60 F. 2d 204..... | 9 |
| <i>Fed. Land Bank v. Bismarck Co.</i> , 314 U. S. 95..... | 11, 30 |
| <i>Ferguson v. Fidelity Union Trust Co.</i> , 24 F. 2d 520..... | 12 |
| <i>First Nat. Bank of Jackson, Miss. v. M'Neel</i> , 238 Fed. 559..... | 8, 16, 33 |
| <i>Gatens Investment Co. v. Commissioner</i> , 36 B. T. A. 309..... | 9, 12 |
| <i>Harrison v. Northern Trust Co.</i> , 317 U. S. 476..... | 37 |
| <i>Helvering v. Bullard</i> , 303 U. S. 297..... | 24 |
| <i>Helvering v. Inter-Mountain Life Insurance Co.</i> , 294 U. S. 686..... | 32 |
| <i>Helvering v. Missouri State Life Ins. Co.</i> , 78 F. 2d 778..... | 9 |
| <i>Helvering v. Stuart</i> , 317 U. S. 154..... | 23 |
| <i>Helvering v. Winmill</i> , 305 U. S. 79..... | 8, 35 |
| <i>Henderson v. Mayor of N. Y.</i> , 92 U. S. 259..... | 25 |
| <i>Hord v. Commissioner</i> , 95 F. 2d 179..... | 9, 12 |
| <i>International H. Co. v. Wisconsin Dept. of Taxation</i> , 243 Wis. 198, 10 N. W. (2d) 169..... | 25 |
| <i>Keith v. Johnson</i> , 271 U. S. 1..... | 9, 10, 18, 19, 20 |
| <i>Kohlsaat v. Commissioner</i> , 40 B. T. A. 528..... | 9, 12 |
| <i>Lawrence v. State Tax Comm.</i> , 286 U. S. 276..... | 25, 27 |
| <i>Lifson v. Commissioner</i> , 98 F. 2d 508..... | 9, 12 |
| <i>Magruder v. Supplee</i> , 316 U. S. 394..... | 8, 9, 11, 18, 19 |
| <i>Merchants Bank Bldg. Co. v. Helvering</i> , 84 F. 2d 478..... | 9 |
| <i>Montreal Mining Co. v. Commissioner</i> , 2 T. C. 688..... | 26 |
| <i>National Bank of Commerce v. Allen</i> , 223 Fed. 472..... | 8, 15, 21, 33 |
| <i>New York Trust Co. v. Eisner</i> , 256 U. S. 345..... | 10, 11 |
| <i>Penney J. C., Co. v. Tax Comm.</i> , 238 Wis. 69..... | 25 |
| <i>Perry v. Commissioner</i> , 32 B. T. A. 513..... | 9 |
| <i>Porter v. United States</i> , 27 F. 2d 882..... | 12, 16, 33 |
| <i>Sabatini v. Commissioner</i> , 98 F. 2d 753..... | 30 |
| <i>Schuylkill Trust Co. v. Penna.</i> , 302 U. S. 506..... | 27 |
| <i>Security First Nat. Bank of Los Angeles v. Commissioner</i> , 36 B. T. A. 72..... | 9, 12 |
| <i>Security Flour Mills, The, v. Commissioner</i> , No. 276, present Term, decided February 28, 1944..... | 26 |
| <i>Shearer v. Commissioner</i> , 48 F. 2d 552..... | 9 |

Cases—Continued.

| | Page |
|---|------------------|
| <i>Small v. Commissioner</i> , 27 B. T. A. 1219..... | 9, 12 |
| <i>State ex rel. Froedtert G. & M. Co. v. Tax Comm.</i> , 221 Wis. 225..... | 21, 22 |
| <i>United States v. Kombel</i> , 286 U. S. 424..... | 9, 10, 18, 19 |
| <i>United States v. Woodward</i> , 256 U. S. 632..... | 9 |
| <i>Walsh-McGuire Co. v. Commissioner</i> , 97 F. 2d 983..... | 9, 12 |
| <i>Wisconsin v. J. C. Penney Co.</i> , 311 U. S. 435..... | 4, 6, 17, 23, 24 |
| <i>Wisconsin Gas & E. Co. v. Wisc. Dep't of Taxation</i> , 243 Wis. 216..... | 17, 26 |

Statutes:

| | |
|--|------------|
| Corporation Excise Tax Act of 1909, c. 6, 36 Stat. 11..... | 8 |
| Current Tax Payment Act of 1943, Public Law 68, 78th Cong., 1st Sess..... | 15 |
| Internal Revenue Code: | |
| Sec. 23 (26 U. S. C., Sec. 23)..... | 32 |
| Sec. 143 (26 U. S. C., Sec. 143)..... | 15, 30 |
| Sec. 1622..... | 15 |
| Sec. 1623..... | 15 |
| Laws of Wisconsin (1935), c. 505, Sec. 3, as amended..... | 39 |
| Revenue Act of 1918, c. 18, 40 Stat. 1057, Sec. 221..... | 15 |
| Revenue Act of 1921, c. 136, 42 Stat. 227: | |
| Sec. 214..... | 7 |
| Sec. 234..... | 7, 32 |
| Revenue Act of 1934, c. 277, 48 Stat. 680, Sec. 23 3, 7, 21, 31, 36, 38 | |
| Wisconsin Statutes (1935), c. 71, Sec. 71.03..... | 17, 21, 42 |

Miscellaneous:

| | |
|---|----------|
| H. Rep. No. 1, 69th Cong., 1st Sess., pp. 19-20 (1939-1 Cum. Bull. (Part 2) 315)..... | 26 |
| Hearings before the Senate Committee on Finance, 67th Cong., 1st Sess., pp. 250-251..... | 33 |
| I. T. 3002, XV-2 Cum. Bull. 142-143 (1936)..... | 16, 43 |
| 5 Mertens, Law of Federal Income Taxation (1942) 43..... | 12 |
| S. Rep. No. 52, 69th Cong., 1st Sess., p. 36 (1939-1 Cum. Bull. (Part 2) 332)..... | 26 |
| S. Rep. No. 275, 67th Cong., 1st Sess., p. 19 (1939-1 Cum. Bull. (Part 2) 181)..... | 34 |
| Treasury Regulations 62, Art. 566..... | 34 |
| Treasury Regulations 65, Art. 131..... | 7 |
| Treasury Regulations 74, Art. 151..... | 7 |
| Treasury Regulations 86: | |
| Art. 23 (c)-1..... | 7, 8, 38 |
| Art. 23 (d)-1..... | 34, 39 |
| Treasury Regulations 111: | |
| Sec. 29.23 (c)-1..... | 8 |
| Sec. 29.23 (d)-1..... | 35 |

In the Supreme Court of the United States

OCTOBER TERM, 1943

No. 565

WISCONSIN GAS & ELECTRIC COMPANY, PETITIONER

v.

THE UNITED STATES OF AMERICA

**ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT
COURT OF APPEALS FOR THE SEVENTH CIRCUIT**

BRIEF FOR THE UNITED STATES

OPINIONS BELOW

The opinion of the District Court (R. 6-8) is reported in 46 F. Supp. 929. The opinion of the Circuit Court of Appeals (R. 20-23) is reported in 138 F. 2d 597.

JURISDICTION

Judgment of the Circuit Court of Appeals was entered on November 8, 1943. (R. 23.) The petition for writ of certiorari was filed on December 30, 1943, and was granted on January 31, 1944. The jurisdiction of this Court rests on Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the Wisconsin Gas and Electric Company, in computing its net income for the year 1935, is entitled under Section 23 (c) or (d) of the Revenue Act of 1934 to a deduction for amounts paid to the State of Wisconsin pursuant to the privilege dividend tax law of that state.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set forth in Appendix A, *infra*, pp. 38-42.

STATEMENT

This is an action against the United States under Section 24, paragraph Twentieth of the Judicial Code, as amended (28 U. S. C., Sec. 41 (20)), to recover federal income taxes for the year 1935 alleged to have been erroneously assessed and collected. (R. 2-3.) The facts were stipulated (R. 5-6) and the findings of fact by the District Court (R. 9-10) are in accord with the stipulation.

The taxpayer is a corporation under the laws of the State of Wisconsin, and its business, that of a public utility corporation, is conducted wholly within that state. (R. 5, 9.) There was no finding that any of its stockholders are non-residents of Wisconsin. (R. 23.) In its federal income tax return for the year 1935 based on the accrual method, it claimed as a deduction the Wisconsin privilege dividend tax of \$3,750 for the year 1935 paid to the State of Wisconsin,

which was assessed and computed in accordance with the Laws of Wisconsin (1935), c. 505, as amended by Laws of Wisconsin (1935), c. 552. (R. 5, 9.) The deduction claimed was disallowed by the internal revenue agent, and this, together with other disallowances, resulted in the determination of an additional tax of \$11,696. (R. 5-6.) The additional tax thus determined was paid by the taxpayer (R. 6, 9) and a timely claim for refund filed, which was rejected (R. 6).

The present action is to recover \$515.63 in federal income taxes due solely to the disallowance of the claimed deduction of the Wisconsin privilege dividend tax. (R. 6, 9.) The District Court rendered an opinion (R. 6-8) sustaining the taxpayer's claim, judgment in its favor (R. 10-11) being entered October 6, 1942. On appeal to the Circuit Court of Appeals for the Seventh Circuit that court on November 8, 1943, rendered its opinion and judgment (R. 20-23) reversing the judgment of the District Court. The case is brought to this Court by a petition for certiorari by the taxpayer granted January 31, 1944.

SUMMARY OF ARGUMENT

I

A taxpayer, in order to deduct under Section 23 (c) "taxes paid or accrued," must show that the tax is imposed upon it. This is the uniform construction of the section in the Treasury Regulations which has been accepted and applied by

this Court. In determining for the above purpose the person upon whom a particular state tax is imposed, the federal courts will be guided by the state statute as interpreted and applied by the courts of the state.

The clear wording of the Wisconsin statute enacting the privilege dividend tax here in question shows that the tax is not imposed upon the corporation but upon the shareholders who receive the dividends. The tax is deducted and withheld from the dividends paid the shareholders. The Wisconsin Supreme Court has held that the tax in question is imposed on the shareholders and not upon the corporation. This was not merely a matter of terminology but was essential to the decisions of that court holding that the tax was not deductible by a corporation for purposes of the state income tax and that a corporation might properly deduct it from preferred dividends which it declared.

The decision of this Court in *Wisconsin v. J. C. Penney Co.*, 311 U. S. 435, is not to the contrary. That decision involved merely the power of the state to impose the tax in question. It held that since the state would have had power to assess an additional tax on the corporate earnings and since the tax in question was confined to such earnings, the tax bore a fiscal relation to protection, opportunities and benefits given by the state, and was therefore within the state's constitutional

power. The Court did not, insofar as the question here involved was concerned, depart from its holdings that for the purpose of tax deductions under the federal income tax law, the incidence of state taxes is to be determined by the state law. The decision of this Court in *Biddle v. Commissioner*, 302 U. S. 573, involved a concept of British tax law, not accepted in the United States, whereby for certain tax purposes the corporation and shareholders are treated as a single entity. The refusal of the Court in that case to adopt that concept and thus to allow a credit to stockholders has no bearing on the instant case, which involves a familiar tax system under which the corporation is the withholding and collecting agent with respect to distinct taxes imposed on the shareholders.

II

Section 23 (d) of the Revenue Act relates to deductions by corporations of taxes paid by them on the shares of the stockholders as property, and is not applicable to the present case. Moreover, deductions under this section are confined to taxes paid by the corporation for which it has not been reimbursed by the shareholders. By the deduction of the privilege dividend tax from the dividends paid to the shareholders, the taxpayer corporation in the present case was reimbursed for the taxes paid by it.

ARGUMENT

I

THE WISCONSIN PRIVILEGE DIVIDEND TAX IS NOT IMPOSED UPON THE CORPORATION BUT UPON THE SHAREHOLDERS, AND IS THEREFORE NOT A TAX DEDUCTIBLE BY THE CORPORATION UNDER THE PROVISIONS OF SECTION 23 (C) OF THE REVENUE ACT

The Government's position in this case can be succinctly and simply stated. Under the federal income tax law and the applicable regulations, taxes may be deducted from gross income only by those persons upon whom they are "imposed." The ascertainment of the person upon whom the tax is imposed is determinable by the decisions of the courts of the state which imposed the tax in question. The Wisconsin privilege dividend tax here involved is by its terms, and as construed by the Supreme Court of Wisconsin, clearly imposed upon the shareholders of the corporation and not upon the corporation itself. Neither the decision of this Court in *Wisconsin v. J. C. Penney Co.*, 311 U. S. 435, sustaining the constitutional power of the state to levy the tax in question, nor the decision of this Court in *Biddle v. Commissioner*, 302 U. S. 573, requires a contrary holding. Therefore the decision of the Circuit Court of Appeals holding that petitioner was not entitled to the deduction claimed is correct and should be affirmed. These points will be discussed in the argument following in their appropriate order.

1. *Taxes are deductible only by the person upon whom they are imposed*

Section 23 of the Revenue Act of 1934 here involved (Appendix A, *infra*, p. 38), insofar as here material, provides that in computing net income there shall be allowed as deductions "Taxes paid or accrued within the taxable year."¹ This tax deduction privilege has been phrased in the identical simple form since the Revenue Act of 1921,² and is so phrased today in the Internal Revenue Code.³ This section of the various revenue laws has, however, for a long period been implemented and construed by the Treasury Regulations promulgated under the authority of Congress. Article 131 of Regulations 65, issued under the Revenue Act of 1924, provided in part as follows: "Taxes are deductible as such only by the person upon whom they are imposed." Article 151 of Treasury Regulations 74, promulgated under the Revenue Act of 1928, provided as follows: "In general taxes are deductible only by the person upon whom they are imposed." The same words have been contained in the Treasury Regulations ever since, including Article 23 (c)-1 of Treasury

¹ This section, as well as the comparable sections of the Revenue Acts for other years and of the Internal Revenue Code, contains certain exceptions to this general rule. The exceptions, however, are not material to the present case.

² See Revenue Act of 1921, c. 136, 42 Stat. 227, Secs. 214 (a) (3) and 234 (a) (3).

³ See Internal Revenue Code, as amended, Sec. 23 (c).

Regulations 86 (Appendix A, *infra* p. 38) applicable to the tax year here in question, and Section 29.23 (c)-1 of the current Treasury Regulations 111, promulgated under the authority of the Internal Revenue Code.⁴ In these circumstances this regulation has the force of law,⁵ as was expressly recognized in *Magruder v. Supplee*, 316 U. S. 394, 396, where this Court said, in considering the statutory provision here involved:

The guiding principle for determining whether a payment satisfying a tax liability is a "tax paid" within the meaning of Section 23 (c) is furnished by the applicable Treasury regulation, which states that "In general taxes are deductible only by the person upon whom they are imposed."

The rule that taxes are deductible under the Revenue Acts only by the person upon whom they are imposed has been consistently applied by this Court, by the Circuit Courts of Appeals

⁴ This principle indeed antedated the federal income-tax laws, having been adopted by the courts under the Corporation Excise Tax Act of 1909, c. 6, 36 Stat. 11, in denying to national banks deductions of taxes paid by them imposed upon the shareholders' property interest in the banks' shares. *Eliot Nat. Bank v. Gill*, 218 Fed. 600 (C. C. A. 1st); *National Bank of Commerce v. Allen*, 223 Fed. 472 (C. C. A. 8th); *First Nat. Bank of Jackson, Miss. v. McNeel*, 238 Fed. 559 (C. C. A. 5th).

⁵ See *Helvering v. Winnmill*, 305 U. S. 79, 83:

"Treasury regulations and interpretations long continued without substantial change, applying to unamended or substantially reenacted statutes, are deemed to have received congressional approval and have the effect of law."

and by the Board of Tax Appeals in respect to a wide variety of taxes, and is today undoubted law.⁶

2. *Whether a particular state tax is imposed upon the taxpayer claiming its deduction is determined by the decisions of the courts of the state which levied the tax*

It is the Government's contention that the Circuit Court of Appeals correctly held that in determining whether the tax here in controversy

⁶ See *United States v. Woodward*, 256 U. S. 632 (federal estate tax); *Keith v. Johnson*, 271 U. S. 1; *United States v. Kohnst*, 286 U. S. 424 (state inheritance tax); *Magruder v. Supplee*, 316 U. S. 394 (state real property tax); *Helvering v. Missouri State Life Ins. Co.*, 78 F. 2d 778 (C. C. A. 8th); *Merchants Bank Bldg. Co. v. Helvering*, 84 F. 2d 478 (C. C. A. 8th); *Walsh-McGuire Co. v. Commissioner*, 97 F. 2d 983 (C. C. A. 6th); *Lifson v. Commissioner*, 98 F. 2d 508 (C. C. A. 8th); *Commissioner v. Plestcheeff*, 100 F. 2d 62 (C. C. A. 9th); *Commissioner v. Coward*, 110 F. 2d 725 (C. C. A. 3d) (state real property taxes); *Hord v. Commissioner*, 95 F. 2d 179 (C. C. A. 6th) (state personal property tax); *Falk Corp. v. Commissioner*, 60 F. 2d 204 (C. C. A. 7th); *Eastern Gas & Fuel A. v. Commissioner*, 128 F. 2d 369, 375 (C. C. A. 1st) (state income taxes); *Shearer v. Commissioner*, 48 F. 2d 552 (C. C. A. 2d) (federal tax on sale of motor vehicle); *Cohan v. Commissioner*, 11 B. T. A. 743, 760; *Eisenberg v. Commissioner*, 11 B. T. A. 574 (federal tax on sale of specified commodities); *Perry v. Commissioner*, 32 B. T. A. 513 (federal gift tax); *Small v. Commissioner*, 27 B. T. A. 1219; *Security First Nat. Bank of Los Angeles v. Commissioner*, 36 B. T. A. 72; *Gatens Investment Co. v. Commissioner*, 36 B. T. A. 309; *Kohlsoat v. Commissioner*, 40 B. T. A. 528, 535 (state property taxes); *Eckstein v. Commissioner*, 41 B. T. A. 746 (state sales tax).

was imposed upon the corporation or its stockholders, the decisions of the Wisconsin Supreme Court construing its own statute were controlling. It has uniformly been held by this Court, by the Circuit Courts of Appeals and by the Treasury Department that the determination whether a state tax for purposes of deduction under the law is "imposed" upon the taxpayer or upon another is dependent upon state law as interpreted by the highest courts of the state.

In *Keith v. Johnson*, 271 U. S. 1, this Court, in deciding that the estate of a decedent was entitled to a deduction in its federal income tax return for the New York transfer taxes paid by it, held itself governed by the last decision of the New York court holding that the transfer tax was "imposed" upon the estate. It said (p. 8):

This court will follow the decisions of the state courts as to the meaning and proper application of the state transfer tax law, any expressions in its earlier decision [i. e., of the state court] to the contrary notwithstanding.

In *United States v. Kombst*, 286 U. S. 424, the Court took the same view in deciding a comparable problem. Section 203 of the Revenue Act of 1916, relating to the federal estate tax, permitted deductions from gross estate of "such other charges against the estate, as are allowed by the laws of the jurisdiction * * * under which the estate is being administered; * * *." The Court had previously determined in *New York*

Trust Co. v. Eisner, 256 U. S. 345, that a succession tax, imposed upon the recipients of the estate, as contrasted with an estate tax, imposed on the estate, was not a deductible charge. In determining whether the California tax was a non-deductible succession tax, or a deductible estate tax, this Court followed the California decisions, saying (286 U. S., at 426), "Whether the California tax was a succession or an estate tax is to be determined by reference to the decisions of its highest court."

The Court adhered to the same criterion in the recent case of *Magruder v. Supplee*, *supra*, which involved the right of a purchaser of Baltimore real estate to deduct under Section 23 (c) of the Revenue Act of 1936, state and city real property taxes paid by him. In determining the person upon whom such taxes were imposed the Court was guided by the state law. "Resort must be had here to the laws of Maryland and of the City of Baltimore to determine upon whom the state and city real estate taxes were imposed." (P. 396.)

The principle thus declared by this Court has been uniformly adhered to by the Circuit Courts

¹ See also *Fed. Land Bank v. Bismarck Co.*, 314 U. S. 95, in which the Court held that a state sales tax could not be applied to sales of commodities to a federal land bank, since under the state decisions the tax was imposed upon the purchaser. "These determinations of the incidence of the tax by the state court are controlling, and respondents concede the point." (P. 99.)

of Appeals and by the Board of Tax Appeals. In determining whether real and personal property taxes are imposed upon the taxpayer who claims the deduction or upon a predecessor in title, resort must be had to the state laws as interpreted by the courts of that state.⁸ The same is true as to state taxes on shares of national and state banks, even though the tax be actually paid by the bank.⁹ Whether a state sales tax is imposed upon the buyer or the seller must also manifestly be determined by resort to state law.¹⁰

3. *The Wisconsin privilege dividend tax by its express terms, and as construed by the Wisconsin Supreme Court, is imposed upon the shareholders of the corporation and not upon the corporation itself*

It is submitted that the Wisconsin statute (Appendix, *infra*, pp. 39-41), providing for the

⁸ *Hord v. Commissioner*, 95 F. 2d 179 (C. C. A. 6th); *Walsh-McGuire Co. v. Commissioner*, 97 F. 2d 983 (C. C. A. 6th); *Lifson v. Commissioner*, 98 F. 2d 508 (C. C. A. 8th); *Commissioner v. Coward*, 110 F. 2d 725 (C. C. A. 3d); *Commissioner v. Plestcheeff*, 100 F. 2d 62 (C. C. A. 9th); *Commissioner v. Rust's Estate*, 116 F. 2d 636 (C. C. A. 4th); *Small v. Commissioner*, 27 B. T. A. 1219; *Security First Nat. Bank of Los Angeles v. Commissioner*, 36 B. T. A. 72; *Kohlsaat v. Commissioner*, 40 B. T. A. 528; *Gatens Investment Co. v. Commissioner*, 36 B. T. A. 309.

⁹ *Porter v. United States*, 27 F. 2d 882 (C. C. A. 9th); *Ferguson v. Fidelity Union Trust Co.*, 24 F. 2d 520 (C. C. A. 3d); *American National Bank of St. Paul v. Commissioner*, 14 B. T. A. 476.

¹⁰ *Eckstein v. Commissioner*, 41 B. T. A. 746, 752; 5 Mertens, *Law of Federal Income Taxation* (1942) 43; *Alabama v. King & Boozer*, 314 U. S. 1, 9-10.

privilege dividend tax here in issue, clearly indicates that the tax is upon the shareholders of the corporation and not upon the corporation itself. The first subsection of the statute provides:

(1) For the privilege of declaring and receiving dividends, out of income derived from property located and business transacted in this state, there is hereby imposed a tax equal to two and one-half per centum of the amount of such dividends declared * * * and paid by all corporations * * *. [Italics supplied.]

The last sentence of the subsection is significant:

Such tax shall be *deducted and withheld* from such dividends payable to residents and nonresidents by the payor corporation. [Italics supplied.]

This provision, that the tax shall be deducted and withheld from the dividends, is repeated in subsections (2) and (3) of the statute:

(2) Every corporation required to deduct and withhold any tax under this section shall, on or before the last day of the month following the payment of the dividend, make return thereof and pay the tax to the tax commission, * * *.

(3) Every such corporation hereby made liable for such tax, shall deduct the amount

of such tax from the dividends so declared."

It will be noticed that the tax is not only on the privilege of declaring dividends but also on receiving them. While it is true that the corporation pays and is made liable to the state for the tax, nevertheless such payment is not in satisfaction of its own liability, but as a withholding agent of the shareholder. This clearly appears from the statutory requirement that the tax "be deducted and withheld." The tax comes out of the dividends receivable by the shareholders and is thus imposed upon them and paid with their funds. If the tax were against the corporation, as the taxpayer contends, there would be no reason whatever for providing that it be deducted from the dividend declared to the shareholders.

That the tax is laid by the statute on the shareholders is, of course, entirely consistent with the statutory responsibility of the corporation for withholding and paying to the state the amounts due. Provisions of a similar character are common in both federal and state revenue laws, and in none of them does the personal liability of the withholding agent establish that the tax in ques-

¹¹ The remaining subsections of the statute relate to the method of determining the portion of the corporation's income derived from property located and business conducted in the state and to administrative provisions, none of which is material to the question here at issue.

tion is "imposed" on it.¹² Compare *Allen v. Regents of the University System of Georgia*, 304 U. S. 439. An example close to the present case is that of state taxes on shares of stock in national banks, for which the bank alone may be made liable to the state ~~for the tax~~. Both under the corporation excise tax of 1909 and under the federal income tax laws prior to their amendment in 1921, it was held that the banks could take no deduction for the taxes paid by them since the tax was not imposed upon them but on the shareholders.¹³

¹² A conspicuous example is the Current Tax Payment Act of 1943, P. L. 68, 78th Cong., 1st Sess., Sec. 2, adding to the Internal Revenue Code, Secs. 1622 and 1623, which require employers to deduct and pay from the wages and salaries of the employees a given percentage of the federal income tax. Another example long present in the Federal Revenue Acts concerns the withholding and payment of income taxes upon nonresident aliens on account of income derived from sources within this country. Sec. 221 (a), Revenue Act of 1918, c. 18, 40 Stat. 1057; Sec. 143 (b) and (c), Internal Revenue Code. Likewise, corporations which issue bonds containing a covenant by the obligor to pay the federal income taxes of the obligee on the interest received from those bonds are required to deduct and pay to the Federal Government a tax equal to two percent of the interest. Sec. 221 (b), Revenue Act of 1918; Sec. 143 (a), Internal Revenue Code. It is expressly provided in Section 1622 (c), added by the Current Tax Payment Act, and in Section 143 (a) (3) of the Internal Revenue Code, that the withholding agent is entitled to no deduction for the taxes withheld and paid by it.

¹³ *Eliot Nat. Bank v. Gill*, 218 Fed. 600 (C. C. A. 1st); *National Bank of Commerce v. Allen*, 223 Fed. 472 (C. C. A.

The Bureau of Internal Revenue ruled specifically on the question here at issue in 1936, soon after the passage of the Wisconsin statute. It concluded that the Wisconsin tax is imposed on the shareholders, and may be deducted by them, not by the corporation, in making federal income tax returns. In L. T. 3002, XV-2 Cum. Bull. 142-143 (1936), *infra*, pp. 42-43, the Income Tax Division stated:

The title of the law and its provisions show that it was the intention of the State legislature to levy an excise tax on the receipt of dividends and to make the corporation declaring and paying the dividend the collector of the tax for and on behalf of the State by requiring the corporation to withhold the tax from the stockholder and to pay the amount withheld to the State tax commission, which in turn pays it into the State treasury.

It is held that the privilege dividend tax is an excise tax imposed upon the stockholder receiving the dividend, who may deduct the amount of the tax in his Federal income tax return. * * *

This is the construction placed upon the statute by the Wisconsin Supreme Court in applying the

8th); *First Nat. Bank of Jackson, Miss. v. M'Nee*, 238 Fed. 559 (C. C. A. 5th); *Porter v. United States*, 27 F. 2d 882 (C. C. A. 9th); *American National Bank of St. Paul v. Commissioner*, 14 B. T. A. 476.

Wisconsin income tax law. *Wisconsin Gas & E. Co. v. Wisc. Dep't of Taxation*, 243 Wis. 216, 10 N. W. (2d) 140; *Blued v. Wisconsin Foundry & Machine Co.*, 243 Wis. 221." From these decisions it is clear that the Wisconsin court considers the privilege dividend tax as a tax imposed on the shareholders and not upon the corporation. The first of these cases involved the deductibility as taxes, under the Wisconsin income tax statute, of Wisconsin privilege dividend taxes withheld and paid by the very taxpayer who is petitioner in the present case. The Wisconsin income tax law (Wisconsin Statutes (1935), Sec. 71.03 (4), Appendix, *infra*, pp. 41-42), allowed a deduction from gross income of "taxes * * * paid during the year upon the business or property from which the income taxed is derived, * * *." In that case, as in this, the taxpayer contended that the tax was imposed upon the corporation and not on the shareholders. In that case, as in this, the taxpayer relied upon the decision of this Court in *Wisconsin v. J. C. Penney Co.*, 311 U. S. 435. The Wisconsin court approached the problem in a manner fully in accord with the opinions of this Court in *Keith*.

¹⁴ The contention of the taxpayer that this Court in *Wisconsin v. J. C. Penney Co.*, 311 U. S. 435, held to the contrary, rests, it is submitted, on an erroneous assumption of what the *Penney* case actually decided. The Wisconsin cases cited were decided after the *Penney* case, and with full consideration of its relevance. The *Penney* case is discussed in Point 4 of this brief, *infra*, pp. 23-27.

v. *Johnson, supra*; *United States v. Kombst, supra*, and *Magruder v. Supplee, supra*. It said (10 N. W. (2d), at 141):

The real question in this case is: on whom is the actual burden of this tax laid? This question can have but one answer. *The statute specifically puts it upon the stockholder.* [Italics supplied.]

After pointing out that the power of the state to pass the tax in question had been authoritatively determined by this Court in the *Penney* case, *supra*, it said:

We are certain of three things: (1) that the burden of the tax is specifically laid upon the stockholder; (2) that the corporation declaring the dividend must deduct the tax from the dividend and may not under any circumstances treat the tax as a necessary expense of doing business; (3) that the power to levy the tax so construed was authoritatively established in the *Penney* case.

It therefore concluded that under the Wisconsin statute no deduction could be taken from the tax in question.

Blid v. Wisconsin Foundry & Machine Co., supra, was an action by a preferred stockholder in a Wisconsin corporation against the corporation to recover the privilege dividend tax deducted and withheld from the preferred dividend declared by the defendant corporation. The court affirmed the decision of the lower court sustain-

ing a demurrer to the complaint. The plaintiff admitted that the language of the statute seemed to place the tax on the stockholder, but contended that such language should be ignored in view of the fact that the corporation alone was made liable for the tax and that no personal liability was imposed upon the stockholder. The apparent contention was that if the tax were against the corporation it would be illegal to deduct the tax from the dividends to which the shareholder was entitled by his contract with the corporation. The Supreme Court affirmed the court below on the grounds set forth in its opinion in the *Wisconsin Gas & Electric Co.* case decided the same day.

These decisions of the Wisconsin Supreme Court are, it is submitted, under the authority of the decisions of this Court in *Keith v. Johnson, supra*, *United States v. Kombst, supra*, and *Magruder v. Supplee, supra*, controlling on the issue here presented.

It may be admitted, as petitioner argues (Br. 15-17), that the deductibility of taxes under a state revenue act is not necessarily determinative of deductibility under the federal law. The Commissioner does not contend to the contrary. The important point is not merely that the tax is not deductible by the corporation under the Wisconsin income tax law, but that the Wisconsin Supreme Court in the cases cited determined that the tax was not upon the corporation but upon the shareholders. In determining the person who is entitled

to deductions of taxes under the Wisconsin statute it appears that the same criteria are applied as in the case of deductions of taxes under the federal statute. The Wisconsin court pointed out that the controlling question was: "Whether this is a tax upon the corporation, in which case it is assumed that it must be regarded as an expense of doing business deductible from gross income, or whether it is a tax upon the stockholders." (243 Wis. at —.) This is merely to state in another form the federal requirement that taxes in order to be deductible must be "imposed" upon the taxpayer claiming their deduction. In deciding that the corporation paying the tax was not entitled to its deduction under the Wisconsin income tax law, the Wisconsin court necessarily held that the tax was not "upon the corporation" or, in the terminology of federal law, was not "imposed" upon it. That determination should, under accepted principles, be followed here, and the tax be held not deductible under the federal act.¹⁵

It is of no significance that the Wisconsin court used the term "burden" in stating that "the burden of the tax is specifically laid upon the stockholder." The statement itself, no less than the opinion as

¹⁵ In this respect the present case is analogous to *Keith v. Johnson, supra*, in which this Court, in applying the federal income tax statute, followed the decision of the New York court holding that, as the New York transfer tax was imposed upon the estate of the decedent, it was a deductible tax for purposes of the state income tax on the estate.

a whole, shows that the term was used as a synonym for the legal incidence of the tax, and not to describe merely its ultimate or transferred economic impact. Cf. *Colorado National Bank v. Bedford*, 310 U. S. 41, 52-53; *National Bank of Commerce v. Allen*, 223 Fed. 472 (C. C. A. 8). It is clear from the decision itself that the court's holding did not turn on any inquiry as to the person upon whom the economic burden of the tax ultimately rested. The case involved appeals by four corporations. One of these corporations, the Wisconsin-Michigan Power Company, instead of deducting the tax from the dividends paid the shareholders, absorbed the tax itself so that the economic burden thereof was borne by the corporation and not by the stockholders. Nevertheless, the Wisconsin court held that the corporation, like the corporations which passed on the burden of the tax to the shareholders, was not entitled under the Wisconsin statute to the deduction of the tax. The Wisconsin income tax law, in allowing deductions for taxes, like the federal law, does not concern itself with the person upon whom the economic burden of the tax ultimately rests. Both under Section 71.03 (4) of the Wisconsin statute and under Section 23 (c) of the Federal Revenue Act, the deduction of the tax is confined to those persons upon whom the tax is in law assessed or imposed. That the Wisconsin court was fully cognizant of the distinction between the two concepts is shown by its original opinion in *State*

ex rel. Froedtert G. & M. Co. v. Tax Comm., 221 Wis. 225, 243, upholding the constitutionality of the Wisconsin tax, where the court specifically stated that it was entirely immaterial "upon whom the burden of it [the tax] ultimately falls."¹⁶

It is submitted that Wisconsin privilege dividend taxes are, both by the wording of the statute which imposes them and by the decisions of the Wisconsin Supreme Court interpreting the statute, clearly not imposed upon the corporation. Hence they are not deductible by the corporation under the Revenue Act as "taxes paid or accrued."

If, however, contrary to the Commission's contention, this Court should deem that the Wisconsin statute or decisions are not clear on the issue here involved, this question, involving as it

¹⁶ The complete quotation from the court's opinion is as follows: (p. 243):

"* * * If the tax is an excise tax, and we hold that it is, it is entirely immaterial upon whom the burden of it ultimately falls. In a sales tax it falls, usually at least, upon the purchaser. In a stamp tax on deeds it usually falls on the seller. In an inheritance tax it falls on the recipient of the property. In the stock transfer tax above referred to it probably fell on the broker consummating the transfer. In a stamp tax on checks it falls on the drawer of the check. In none of the cases is it a personal property tax against the person upon whom the burden of it ultimately falls."

The court also took pains to point out: "we did not in the original opinion take the position that the tax is necessarily one against the corporation." In none of its later decisions has the court receded from this position.

does a matter of a local statute, is of the kind which this Court has suggested may ordinarily be left to the Circuit Court of Appeals which is more conversant with the local law. See *Helvering v. Stuart*, 317 U. S. 154, 162-163.

4. *The decisions of this court in Wisconsin v. J. C. Penney Co. and Biddle v. Commissioner are not applicable to the present case*

The contention that this Court in *Wisconsin v. J. C. Penney Co.*, 311 U. S. 435, held that the Wisconsin privilege dividend tax was assessed against the corporation on its Wisconsin earnings and that the holding is conclusive of the question here presented rests, it is submitted, on a misconception of what this Court actually decided in that case. That case involved only the power of the State of Wisconsin to levy the tax in question. As the Government understands that decision, this Court, in describing the "practical operation of this legislation" as the levy of "an additional tax on corporate earnings within Wisconsin" (311 U. S. at 442), did not undertake to determine that as between corporation and shareholders the legal incidence of the tax was on the former. The Court reasoned that since the State of Wisconsin would have had the power to levy a tax upon such earnings, and since the tax in question was confined to such earnings, it came within that constitutional power of the

state, even though the tax itself was denominated one "For the privilege of declaring and receiving dividends" and had thus been characterized by the supreme court of the state. In thus upholding the tax in question, this Court acted on well recognized principles. The criterion for determining the power of a state to levy taxes is, as this Court stated (311 U. S. at p. 444):

whether the taxing power exerted by the state bears fiscal relation to protection, opportunities and benefits given by the state. The simple but controlling question is whether the state has given anything for which it can ask return.

In that case this Court found such protection, opportunity and benefits in the grant of the "substantial privilege of carrying on business in Wisconsin." (Pp. 444-445.) The "descriptive pigeonhole" into which the state court put the tax was entirely immaterial. The decision, therefore, simply stands for the proposition that the state's power to tax depends upon the "benefit and protection conferred by the taxing sovereignty" in respect to the tax in question. *Curry v. McCannless*, 307 U. S. 357, 368. The answer to this constitutional question is not dependent upon the particular form which the tax in question may take.¹⁷

That this is all that the Court decided in the *Penney* case is shown by its reference (pp. 443-

¹⁷ See *Helvering v. Bullard*, 303 U. S. 297, 301.

444) to *Henderson v. Mayor of N. Y.*, 92 U. S. 259, and to *Lawrence v. State Tax Comm.*, 286 U. S. 276, 280. The first of these cases held unconstitutional a New York statute because its practical effect was to impose a tax on foreign commerce, though the statute in question was phrased in the language of a police measure. The second upheld a state income tax on the out-of-state earnings of a state resident since the Court found, as far as the question of power to tax was concerned, no distinction between such a tax and a state property tax on the intangibles of its citizens, wherever the intangibles might be considered to be located.

The grounds upon which this Court relied in sustaining the validity of the Wisconsin tax have not led the Supreme Court of Wisconsin to hold that the tax in question is a tax upon the corporation. On remand of the *Penney* case, that court adhered to the position that the tax is a tax "on the privilege of declaring and receiving a dividend", and in "no sense and to no extent whatever, is it a tax upon the income of the corporation." *J. C. Penney Co. v. Tax Comm.*, 238 Wis. 69, 73. The Wisconsin court later said in *International H. Co. v. Wisconsin Dept. of Taxation*, 243 Wis. 198, 10 N. W. (2d) 169, 172: "As we read the opinion of the United States Supreme Court, we discover no attempt by the court to usurp the function of this court so far as construing or labeling this tax is concerned." The court, correctly in

our view, construed the opinion of this Court in the *Penney* case as merely ascertaining the "factual basis" upon which the validity of the Wisconsin tax depended. Moreover, as has been shown, the Wisconsin court in *Wisconsin Gas & E. Co. v. Wisc. Dept. of Taxation*, *supra*, upon full consideration of the *Penney* case, specifically held that the Wisconsin privilege dividend tax is imposed on the stockholders and not upon the corporation." The taxpayer in relying upon the Wisconsin decisions that this is a tax on the privilege of declaring and receiving dividends,

¹⁸ The contrary opinion of the district court in the present case (R. 6-8), and the opinion of the Tax Court in *Montreal Mining Co. v. Commissioner*, 2 T. C. 688, both of which rely upon the decision of this Court in the *Penney* case, are not persuasive. The opinion of the district court was promulgated prior to the decision of the Wisconsin court in the *Wisconsin Gas & Electric Co.* case. Although the opinion of the Tax Court was published after that decision, the case was submitted and briefed prior thereto, and the Tax Court makes no reference to it. The decision of the Tax Court does not rest upon its independent determination of the issue presented, but upon the assumed authority of the *Penney* case. Cf. *Commissioner v. Heininger*, No. 63, present Term, decided December 20, 1943. Moreover, this is not a field in which the Tax Court's experience and special qualifications entitle its decisions to more weight than the judgments of other qualified tribunals. The ultimate question is one of statutory construction and even where the meaning of a federal statute is involved the Tax Court's decisions are specifically made reviewable. H. Rep. No. 1, 69th Cong., 1st Sess., pp. 19-20 (1939-1 Cum. Bull. (Part 2) 315, 328); S. Rep. No. 52, 69th Cong., 1st Sess., p. 36 (1939-1 Cum. Bull. (Part 2) 332, 359). *The Security Flour Mills v. Commissioner*, No. 276, present Term, decided February 28, 1944.

cannot ignore the correlative holding that the tax is on the shareholders and not on the corporation.

Acceptance by this Court of the Wisconsin court's characterization of the tax as one imposed upon the shareholders will not affect the previous decision of this Court that the tax is within the constitutional power of the state. Whether the tax be regarded as imposed upon the corporation or upon the shareholders, the source of the tax is the earnings of a corporation in Wisconsin. Since such earnings depend upon the privilege granted to the corporation by the State of Wisconsin, the constitutional power of the state to levy the tax is clear. This is particularly true of the present case, where the corporation is one created by the State of Wisconsin, and where it has not been found that any of the shareholders were nonresidents of the state (see opinion of the Circuit Court of Appeals, R. 23). But in any event, since the corporation here involved was a Wisconsin corporation, the power of the state to tax the interest of the shareholders, whether by a property tax or by a tax on the receipt of dividends, is incontrovertible. See *Corry v. Baltimore*, 196 U. S. 466; *Schuykill Trust Co. v. Penna.*, 302 U. S. 506, 514; *Lawrence v. State Tax Comm.*, 286 U. S. 276.

The decision below also is not opposed to the decision of this Court in *Biddle v. Commissioner*, 302 U. S. 573, relied upon by the taxpayer. That

case concerned the right of a taxpayer to a credit for "the amount of any income * * * taxes paid or accrued during the taxable year to any foreign country" as provided in Section 131 (a) (1) of the Revenue Act of 1928, as well as the alternative claim of the taxpayer for deduction of "taxes paid or accrued" under Section 23 (c) of the same Act. The taxpayer claimed under those sections an allowance of certain taxes asserted to constitute "income taxes" imposed upon her under the British income tax act. The British law imposed a standard or normal income tax on the corporation. It imposed a surtax on the shareholders, which was measured not only by the dividends paid to the shareholder but by an additional amount, called a tax "appropriate to" the dividend, computed at the normal rate. The surtax paid by the shareholders was concededly allowable as a credit and deduction under the Federal revenue act. The question related solely to the tax "appropriate to" the dividend, which was not a tax paid either by the shareholders or by the corporation on their behalf save as the ordinary corporate income tax payable for the year in which the corporate income was earned may have corresponded to the item in question. In including this item in the surtax base for the shareholders, and in giving them in certain circumstances a right of refund with respect to the ordinary corporate tax, the British law to that extent treated the corporation and its

shareholders as a single entity. As this Court explained, that treatment was in recognition of the conception that the stockholders in any event bear the economic burden of the corporate tax. See 302 U. S., p. 581. "Our revenue laws," this Court added, "give no recognition to that conception" (*Ibid.*). Consequently the tax "appropriate to" the dividends could not be regarded for purposes of our revenue act as a tax imposed on the shareholders.

That case furnishes no basis for disregarding the nature of the tax here involved, as established by the decisions of the Wisconsin court. In the *Biddle* case the only taxes paid to the Crown were the normal corporate income tax and the individual surtax, and for the latter the shareholders received credit under our law. The present case involves a transaction whereby the corporation is required to deduct from dividends otherwise due to the shareholders an amount to be paid over to the public treasury, in addition to the ordinary corporate income tax whose economic burden is borne by the shareholders and which alone was involved in the *Biddle* case. The *Biddle* case was concerned with a claimed credit based on a system of corporate taxation wholly foreign to our own; the present case involves a system which is by no means unfamiliar, which has been authoritatively explained by the state court, and by which there is imposed upon one

class of taxpayers a tax which is collected by requiring the taxpayers' obligors to withhold the tax and themselves pay it to the Government.

The phrase in the *Biddle* opinion that our law does not treat "as taxpayers those upon whom no legal duty to pay the tax is laid" (p. 581) cannot be wrenched from the facts in respect of which it was uttered. The federal law frequently treats as taxpayers those upon whom no personal liability for the tax is imposed. Owners of real estate who pay the taxes imposed upon the land are treated as taxpayers and are entitled to deduct such taxes in their federal income tax returns though the tax is solely a lien upon the land and no personal liability to pay it is imposed on anyone. *Commissioner v. Coward*, 110 F. 2d 725 (C. C. A. 3d). Also, the Federal Government treats as taxpayers citizens of foreign countries residing abroad, where their income is attributable to sources in this country, even though for obvious reasons no personal duty to pay the tax is imposed upon them. See Sec. 143 (b) and (c), Internal Revenue Code; *Sabatini v. Commissioner*, 98 F. 2d 753 (C. C. A. 2d). And in deciding whether state taxes on services rendered or on goods sold place an unconstitutional exaction on federal agencies, this Court does not regard as decisive the entity on whom the duty rests to make the actual payment to the state. *Colorado Bank v. Bedford*, 310 U. S. 41; *Fed. Land Bank v. Bismarck Co.*, 314 U. S. 95. In any event, the Wisconsin privilege

dividend tax, since it is required to be withheld and deducted from the dividend payable to the shareholders, is not only imposed upon them, but collected from their funds. It is their tax and not a tax of the corporation.

II

THE TAXPAYER IS NOT ENTITLED UNDER SECTION 23 (d) OF THE REVENUE ACT OF 1934 TO A DEDUCTION OF THE WISCONSIN PRIVILEGE DIVIDEND-TAX

Petitioner raises the question whether, assuming that the Wisconsin privilege dividend tax is imposed upon the shareholders, the corporation paying it is nevertheless entitled to a deduction of tax under Section 23 (d) of the Revenue Act of 1934. That section provides (Appendix A, *infra*, p. 38):

The deduction for taxes allowed by subsection (c) shall be allowed to a corporation in the case of taxes imposed upon a shareholder of the corporation upon his interest as shareholder which are paid by the corporation without reimbursement from the shareholder, * * *

It is submitted that this section has no application to the Wisconsin privilege dividend tax, in the light of its clear wording, its legislative history, and the construction uniformly given to it by the Treasury Regulations. The inapplicability of the section rests on the fact (a) that the present tax is not on the "interest" of the shareholders as

such, and (b) that the corporation in substance receives "reimbursement" from the shareholders by deducting the amount of the tax from the dividends paid. Either ground requires the conclusion that section 23 (d) has no application.

A. The deduction is restricted by the words of the statute to "taxes imposed upon a shareholder of the corporation upon his *interest* as shareholder." (Italics supplied.) This, it is submitted, refers to property taxes upon the shares of stock imposed upon the shareholders and not to an excise tax in respect of dividends, such as the present tax is declared to be. But even though the statute be considered ambiguous, the doubt must be resolved in favor of the Government since the section in question is an allowance of a deduction. "The rule that ambiguities in statutes imposing taxes are to be resolved in favor of taxpayers does not apply. Deductions are allowed only when plainly authorized." *Helvering v. Inter-Mountain Life Insurance Co.*, 294 U. S. 686, 689. This provision was first enacted by Section 234 (a) of the Revenue Act of 1921 and has remained in substantially the same form down to and including Section 23 (d) of the Internal Revenue Code. The occasion and purpose of the enactment are quite clear. It will be recalled that prior to this statute it had been held that national and other banks were not entitled to a deduction for state taxes upon the shares of stock in those

banks even though the tax was collected from and paid by the bank. *Eliot Nat. Bank v. Gill*, 218 Fed. 600 (C. C. A. 1st); *National Bank of Commerce v. Allen*, 223 Fed. 472 (C. C. A. 8th); *First Nat. Bank of Jackson, Miss. v. M'Neel*, 238 Fed. 559 (C. C. A. 5th); *Porter v. United States*, 27 F. 2d 882 (C. C. A. 9th); *American National Bank of St. Paul v. Commissioner*, 14 B. T. A. 476. The provision here in question was obviously intended by Congress to allow the banks to take the deduction denied them by these cases. The provision was introduced into the federal revenue laws by a Senate amendment to the Revenue Bill for 1921. In the Hearings before the Committee on Finance of the United States Senate, 67th Cong., 1st Sess., pp. 250-251, Dr. T. S. Adams, Technical Advisor to the Treasury, made the following statement:

Now, Senator Smoot, reverting to your proposition, the Bankers' Association are asking that they be allowed to claim deduction for State and local property taxes which they pay. The banks pay these taxes for and on behalf of their stockholders. The taxes, you will remember, are on the stockholders. The bank voluntarily assumes it and pays it. The banks now want to claim a deduction for it. They do it almost universally.

This amendment was adopted by the Committee and thus found its way into the Revenue Act.

While the Senate Committee Report on that Bill is phrased in language broad enough to include the deduction of all taxes on shareholders paid by the corporation," it is submitted that the amendment confining the deduction to taxes "imposed upon a shareholder of the corporation upon his interest as shareholder" is limited to taxes upon the shares as property and does not include the tax here in question.

This is the uniform construction given to the statute by the Treasury Regulations. Treasury Regulations 62, promulgated under the Revenue Act of 1921, provided in Article 566:

Under the Revenue Act of 1921 banks or other corporations paying taxes assessed against their stockholders *on account of their ownership of the shares of stock issued by such corporations*, without reimbursement from such shareholder or member, may deduct the amount of taxes so paid. [Italics supplied.]

This regulation is identical with Article 23 (d)-1 of Regulations 86 (Appendix A, *infra*, p. 39), promulgated under the Revenue Act of 1934, applica-

¹⁹ S. Rep. No. 275, 67th Cong., 1st Sess., p. 19 (1939-1 Cum. Bull. (Part 2) 181, 194):

"Section 234 authorizes corporations to take deductions similar to those accorded individuals by the terms of section 214, with the following provisions applicable only to corporations: (1) Corporations (particularly banks) are permitted to deduct certain taxes paid by them for or on behalf of their shareholders or members; * * *

ble to the present case. It is contained in identical form in all the Regulations promulgated since the section was first introduced into the Act. See Regulations 111, promulgated under the Internal Revenue Code, Sec. 29.23 (d)-1. This regulation clearly confines the deduction to taxes assessed against shareholders on account of their ownership of the shares of stock, and is entitled to the effect of law. See *Helvering v. Winmill*, 305 U. S. 79, 83.

The only attempt by a corporation to extend this deduction to taxes other than those imposed on stock as property, so far as our research has discovered, was in *Eastern Gas & Fuel A. v. Commissioner*, 128 F. 2d 369 (C. C. A. 1st). In that case the taxpayer association, a so-called Massachusetts trust, had agreed in its declaration of trust to pay the Massachusetts income taxes levied on its members on account of dividends declared by the association. The court denied that the association was entitled to a deduction for such taxes under Section 23 (d), saying (p. 375):

Section 23 (d) allows a deduction to a corporation in the case of taxes "imposed upon a shareholder of the corporation upon *his interest as shareholder* which are paid by the corporation without reimbursement from the shareholder * * *." (Italics supplied.) It is clear from the regulations that the use of the term "interest"

relates to a tax upon the ownership of stock and not to the income derived therefrom. Art. 23 (d), Regulations 86, 1934; 3 Paul & Mertens, *supra*, Secs. 25.28, 25.30. We are satisfied that this is the correct interpretation of Section 23 (d). * * *

B. Moreover, and perhaps of greater importance, Section 23 (d) of the Revenue Act confines the corporation's deductions to taxes paid by it on behalf of its shareholders "without reimbursement from the shareholder." The obvious purpose of the provision is to confine the deduction to taxes the burden of which is borne by the corporation.

The taxpayer in the instant case has not shown that it bore the burden of the tax, and since the tax was assessed in accordance with the Wisconsin statute (R. 5), it must be assumed that the provisions of that statute were followed and that the tax was in fact withheld from the dividends paid. Such deduction was in effect a "reimbursement" of the corporation for the tax paid, though it occurred through the medium of a withholding of the tax from the amounts due the shareholders, instead of through the more circuitous method of a payment by the corporation to the shareholders of the entire dividend and a repayment by them of the tax paid by the corporation. The specific purpose of the statutory qualification of the right to deduct taxes is clear, and its operation will not be

avoided because the corporation was reimbursed by a direct instead of an indirect method.²⁰

CONCLUSION

The decision of the Circuit Court of Appeals is correct and should be affirmed.

Respectfully submitted.

CHARLES FAHY,

Solicitor General.

SAMUEL O. CLARK, Jr.,

Assistant Attorney General.

SEWALL KEY,

J. LOUIS MONARCH,

RAY A. BROWN,

Special Assistants to the Attorney General.

MARCH 1944.

²⁰*Cf. Harrison v. Northern Trust Co.*, 317 U. S. 476. There this Court held that residuary bequests to charities were not deductible from the federal estate tax to the extent of the entire amount of the residue, but only on that amount with the federal estate tax deducted therefrom. In so holding the Court refused to give a literal construction to the words taxes "payable * * * out of the bequests" in Section 807 of the Revenue Act of 1932, relying on the purpose of Congress as disclosed in the legislative history of the Act to disallow taxes which in fact reduced the charitable bequests.

APPENDIX A

Revenue Act of 1934, c. 277, 48 Stat. 680:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * *

(c) *Taxes Generally.*—Taxes paid or accrued within the taxable year, except—[exceptions not pertinent to the instant case]

* * * * *

(d) *Taxes of Shareholder Paid by Corporation.*—The deduction for taxes allowed by subsection (c) shall be allowed to a corporation in the case of taxes imposed upon a shareholder of the corporation upon his interest as shareholder which are paid by the corporation without reimbursement from the shareholder, but in such cases no deduction shall be allowed the shareholder for the amount of such taxes.

Treasury Regulations 86, promulgated under the Revenue Act of 1934:

ART. 23 (c)-1. *Taxes.*—Subject to the exceptions stated in this article and articles 23 (c)-2 and 23 (c)-3, taxes imposed by the United States, any State or Territory, or political subdivision of either, possessions of the United States, or foreign countries, are deductible from gross income for the year in which paid or accrued (see section 43). Estate, inheritance, legacy, succession, and gift taxes and Federal income, war-profits, and excess-profits taxes are not deductible.

from gross income. Income, war-profits, and excess-profits taxes imposed by the authority of any foreign country or possession of the United States are deductible from gross income in cases where the taxpayer does not signify in his return his desire to have to any extent the benefits of section 131 (relating to credit for taxes of foreign countries or possessions of the United States). See generally articles 131-1 to 131-8 as to tax credits. Postage is not a tax. Amounts paid to States or Territories under secured debts laws in order to render securities tax exempt are deductible. Automobile license fees are ordinarily taxes. In general taxes are deductible only by the person upon whom they are imposed. As to tax paid at the source on interest from tax-free covenant bonds, see section 143 (a) (3).

ART. 23 (d)-1. [as amended by T. D. 4585, XIV-2 Cum. Bull. 54 (1935)] *Tax on bank or other stock.*—Banks or other corporations paying taxes assessed against their shareholders on account of their ownership of the shares of stock issued by such corporations without reimbursement from such shareholders may deduct the amount of taxes so paid. The Act specifically provides, however, that in such cases the shareholders may not deduct the amount of the taxes. The amount so paid should not be included in the income of the shareholder.

Laws of Wisconsin (1935), c. 505:

SEC. 3. *Privilege dividend tax.* [as amended by Laws of Wisconsin (1935), c. 552, Sec. 1] (1) For the privilege of declaring and receiving dividends, out of income derived from property located and business transacted in this state, there is

hereby imposed a tax equal to two and one-half per centum of the amount of such dividends declared * * * and paid by all corporations (foreign and local) after the passage and publication of this act and prior to July 1, 1937. Such tax shall be deducted and withheld from such dividends payable to residents and nonresidents by the payor corporation.

(2) Every corporation required to deduct and withhold any tax under this section shall, on or before the last day of the month following the payment of the dividend, make return thereof and pay the tax to the tax commission, reporting such tax on the forms to be prescribed by the tax commission.

(3) Every such corporation hereby made liable for such tax, shall deduct the amount of such tax from the dividends so declared.

(4) In the case of corporations doing business within * * * and without the state of Wisconsin, such tax shall apply only to dividends declared and paid out of income derived from business transacted and property located within the state of Wisconsin. The amount of income attributable to this state shall be computed in accordance with the provisions of chapter 71. In the absence of proof to the contrary, such dividends shall be presumed to have been paid out of earnings of such corporation attributable to Wisconsin under the provisions of chapter 71, for the year immediately preceding the payment of such dividend. If a corporation had a loss for the year prior to the payment of the dividend, the tax commission shall upon application, determine the portion of such dividend paid out of corporate surplus and

undivided profits derived from business transacted and property located within the state.

(5) Dividends paid by a subsidiary corporation to its parent shall not be subject to the tax herein imposed provided that the subsidiary and its parent report their income for taxation under the provisions of chapter 71 on a consolidated income return basis, or both corporations report separately.

(6) The provisions of this section shall not apply to dividends declared and paid by a Wisconsin corporation out of its income which it has reported for taxation under the provisions of chapter 71, * * * *to the extent that the business of such corporation consists in the receipts of dividends from which a privilege dividend tax has been deducted and withheld* and the distribution thereof to its stockholders.

(7) For the purposes of this section dividends shall be defined as in section 71.02, except that the tax herein imposed shall not apply to stock dividend or liquidating dividends.

(8) The tax hereby levied, if not paid within the time herein provided, shall become delinquent and when delinquent shall be subject to a penalty of two per cent on the amount of the tax and interest at the rate of one-half per cent per month until paid.

(9) The tax hereby imposed shall, when collected by the tax commission, be paid by it into the state treasury.

The Act was further amended retroactively by Laws of Wisconsin (1937), c. 233, Secs. 1 and 4. The amendments, however, are not pertinent to the present case.

Wisconsin Statutes (1935), c. 71:

71.03 Deductions from gross income of corporations.—Every corporation, joint stock company or association shall be allowed to make from its gross income the following deductions:

* * * *

(4) Taxes other than special improvement taxes paid during the year upon the business or property from which the income taxed is derived, including therein taxes imposed by the state of Wisconsin and the government of the United States as income, excess or war profits and capital stock taxes, including taxes on all real property which is owned and held for business purposes whether income producing or not, provided that such portion of the deduction for federal income and excess profits taxes as may be allowable shall be confined to cash payments made within the year covered by the income tax return, and provided further that deductions for income taxes paid to the United States government shall be limited to taxes paid on net income which is taxable under this chapter; and provided further that income taxes imposed by the state of Wisconsin shall accrue for the purpose of this subsection only in the year in which such taxes are assessed.

APPENDIX B

I. T. 3002, XV-2 Cum. Bull. 142-143 (1936):

Advice is requested whether, for Federal income tax purposes, the corporation paying a dividend or the stockholder receiving it is entitled to deduct the privilege dividend tax of $2\frac{1}{2}$ per cent imposed by the State of Wisconsin under section 3 of chapter 505, Laws of Wisconsin, 1935.

* * * * *

The title of the law and its provisions show that it was the intention of the State legislature to levy an excise tax on the receipt of dividends and to make the corporation declaring and paying the dividend the collector of the tax for and on behalf of the State by requiring the corporation to withhold the tax from the stockholder and to pay the amount withheld to the State tax commission, which in turn pays it into the State treasury.

Section 23 (c) of the Revenue Act of 1934 provides that in computing net income there shall be allowed as deductions taxes paid or accrued within the taxable year, with certain exceptions not here material. Article 23 (c)-1 of Regulations 86, relating to the Revenue Act of 1934, provides that in general taxes are deductible only by the person upon whom they are imposed.

It is held that the privilege dividend tax is an excise tax imposed upon the stockholder receiving the dividend, who may deduct the amount of the tax in his Federal income tax return. The stockholder, however, should report in his return the full amount of the dividend, including the tax withheld.

SUPREME COURT OF THE UNITED STATES.

No. 565.—OCTOBER TERM, 1943.

| | |
|--|---|
| Wisconsin Gas and Electric Com- pany, Petitioner, vs. The United States of America. | } On Writ of Certiorari to the United States Cir- cuit Court of Appeals for the Seventh Circuit. |
|--|---|

[May 29, 1944.]

Mr. Justice RUTLEDGE delivered the opinion of the Court.

Wisconsin Gas and Electric Company is a Wisconsin corporation engaged in public utility and associated operations wholly within that State. In 1935 it declared a dividend from its public utility earnings, and in accordance with the requirements of Wisconsin's Privilege Dividend Tax Act [Wisconsin Laws of 1935, c. 565, § 3; c. 552], it paid to the State two and one-half per cent of the amount of dividends thus declared. It now claims this sum, \$3,750, as a deduction from its gross income for 1935 for federal income tax purposes.

After the claim was disallowed and a deficiency assessed, the company paid the tax and brought this suit for refund under 28 U. S. C. § 41(20). The District Court was of the opinion that the decision in *Wisconsin v. J. C. Penney Co.*, 311 U. S. 435, required permitting the deduction under Section 23(e) of the Revenue Act of 1934, 48 Stat. 680, 688. It therefore gave judgment for the company. 46 F. Supp. 929. The Circuit Court of Appeals disagreed on this question and, holding the deficiency correctly determined, reversed the judgment. 138 F. 2d 597. We granted certiorari, 321 U. S. —, because of the claimed conflict with the *Penney* case and the importance of the question in the administration of the revenue laws.

Petitioner's claim for a refund rests on the assertion it was entitled to deduct the Privilege Dividend Tax payments under either Section 23(e) or Section 23(d) of the Revenue Act of 1934, 48 Stat. 680, 688, 689.

Section 23(e) allows a taxpayer to deduct from gross income "taxes paid or accrued within the taxable year." The relevant

Treasury Regulation, which is of long standing,¹ includes among "taxes paid" those imposed by any State, and provides: "In general taxes are deductible only by the person upon whom they are imposed." The question in this branch of the case, therefore, comes down to whether the Privilege Dividend Tax is "imposed" upon the corporation declaring the dividends.

Resolution of that question requires examination of the Wisconsin statute and its application and interpretation by the courts of that State. *Keith v. Johnson*, 271 U. S. 1; *United States v. Kombst*, 286 U. S. 424; *Magruder v. Supplee*, 316 U. S. 394. In 1935 the state Act² provided:

(1) For the privilege of declaring and receiving dividends, out of income derived from property located and business transacted in this state, there is hereby imposed a tax equal to two and one-half per centum of the amount of such dividends declared and paid by all corporations (foreign and local) after the passage and publication of this act and prior to July 1, 1937. Such tax shall be deducted and withheld from such dividends payable to residents and nonresidents by the payor corporation.

(2) Every corporation required to deduct and withhold any tax under this section shall, on or before the last day of the month following the payment of the dividend, make return thereof and pay the tax to the tax commission, reporting such tax on the forms to be prescribed by the tax commission.

(3) Every such corporation hereby made liable for such tax, shall deduct the amount of such tax from the dividends so declared.³

The tax is aimed at corporate earnings "derived from property located and business transacted in" Wisconsin. Doubtless all taxes on corporate earnings are, to a greater or lesser extent, translated into economic burdens upon the shareholder. And not all such taxes can be said, for that reason, to be "imposed" upon the shareholder. Cf. *Biddle v. Commissioner*, 302 U. S. 573. However, here the burden is placed upon him, not derivatively as through an income tax upon the corporation, but directly and

¹ Treasury Regulation 86, Art. 23(c)-(1); cf. Treasury Regulation 65, Art. 131; Treasury Regulation 69, Art. 131; Treasury Regulation 74, Art. 151; Treasury Regulation 77, Art. 151.

² Wisconsin Laws of 1935, c. 505, § 3 as amended by Wisconsin Laws of 1935, c. 552. The Act was subsequently amended (Wisconsin Laws of 1937, c. 233; c. 309, § 3; Wisconsin Laws of 1939, c. 198; Wisconsin Laws of 1941, c. 63, § 3; Wisconsin Laws of 1943, c. 367, § 2), but the amendments leave the present question unaffected.

³ The Act is set out in full in *Wisconsin v. J. C. Penney Co.*, 311 U. S. 435, at note 1.

exclusively. While corporate earnings are the target of this tax, its specific thrust, according to the Wisconsin Supreme Court, is at their transfer as dividends to the shareholder, rather than at their receipt as income by the corporation. *J. C. Penney Co., v. Tax Commission*, 238 Wis. 69. It is not imposed until dividends are declared. When imposed it is to be deducted and withheld not from earnings received by the corporation, but "from the dividends so declared." The sums thus paid to the State are to be deducted from the fixed dividends owed to the preferred stockholder who cannot recover his loss from the corporation. *Blued v. Wisconsin Foundry & Machine Co.*, 243 Wis. 221. And the corporation which seeks to leave the stockholder's dividend whole by absorbing the tax itself receives no credit therefor under those provisions of the Wisconsin income tax law comparable to Section 23(c), because the State "puts the burden of this tax upon the stockholder and not upon the corporation." *Wisconsin Gas & Electric Co. v. Wisconsin Department of Taxation*, 243 Wis. 216.

That Wisconsin has made the corporation its tax collector by requiring it to withhold payment of a portion of the dividends and to turn that portion over to the State does not make the tax one "imposed" upon the corporation, at least under Section 23(c) and the relevant Treasury Regulation. Compare *Eliot National Bank v. Gill*, 218 Fed. 600 (C. C. A.); *Porter v. United States*, 27 F. 2d 882 (C. C. A.) The fact is that the tax is extracted from fixed dividends owed to the stockholder, not merely from his common interest in corporate earnings. Under Wisconsin decisions the impact of the tax is focused narrowly and falls independently upon each recipient of the dividend without affecting the tax burden of the corporation or other shareholders. The operation thus disclosed for the tax amply sustains the emphatic declaration of the Wisconsin Supreme Court that it is imposed upon the shareholder, not upon the corporation. This view is complemented by the interpretation of the Bureau of Internal Revenue that the tax payments, although formally made by the corporation, are deductible by the shareholder.⁴ We conclude that the Privilege Dividend Tax is not "imposed" upon petitioner and therefore payments of it are not deductible under Section 23(c).

There is of course no question in this case that Wisconsin has the power, under the Federal Constitution, to impose this tax.

⁴ I. T. 3002, XV-2 Cum. Bull. 142-143 (1936).

That question was involved in *Wisconsin v. J. C. Penney Co.*, 311 U. S. 435, where this Court was concerned with dividends declared by a foreign corporation doing a local business in Wisconsin. The decision was that the relationship of the State to the enterprises there shown to have been carried on within its boundaries and under the protection of its police power was such that its taxing power could constitutionally reach earnings derived from those operations, regardless of how the impost was characterized by the State. The State's power to tax earnings of that character is not dependent upon whether the tax is hinged on the receipt of them as corporate income or on the transfer and receipt of them as dividends. Nor does it depend upon whether the tax here involved is "imposed" upon the corporation or upon the stockholder. *International Harvester Co. v. Wisconsin Department of Taxation*, No. 620, decided this day; *Minnesota Mining and Manufacturing Co. v. Wisconsin Department of Taxation*, No. 621, decided this day. In this case, where the earnings of a Wisconsin corporation doing business solely in Wisconsin are the source of the dividends, the State's power to tax their transfer and impose that tax upon the stockholder cannot be doubted.

Petitioner also urges that if the payments are not deductible from its gross income under Section 23(c), they are deductible under Section 23(d) as "taxes imposed upon a shareholder of the corporation upon his interest as shareholder which are paid by the corporation without reimbursement from the shareholder."⁵ The Government responds that the Privilege Dividend Tax is not the kind of tax "upon his interest as shareholder" which Section 23(d) contemplates, and that in any event it is not one which is "paid by the corporation without reimbursement from the shareholder" within the meaning of the section. Since we think the Government is correct in the latter contention we have no occasion to consider whether this tax is one "upon his interest as shareholder."

The origins of the present Section 23(d) in the Revenue Act of 1921 disclose that its adoption was prompted by the plight of

⁵ Section 23(d) provides: "Taxes of Shareholder Paid by Corporation.—The deduction for taxes allowed by subsection (c) shall be allowed to a corporation in the case of taxes imposed upon a shareholder of the corporation upon his interest as shareholder which are paid by the corporation without reimbursement from the shareholder, but in such cases no deduction shall be allowed the shareholder for the amount of such taxes."

various banking corporations which paid and voluntarily absorbed the burden of certain local taxes imposed upon their shareholders, but were not permitted to deduct those payments from gross income.⁶ This history suggests it is the voluntary assumption of the burden of the tax, rather than acting as tax collector and paying it for another on whom the burden falls; which underpins the deduction. And this is plainly demonstrated by the requirement that to be entitled to the deduction the corporation must not be reimbursed by the shareholder for paying the tax. To pay the tax with sums which have been deducted and withheld from dividends declared and distributed amounts to obtaining the reimbursement which renders the deduction unavailable. Hence petitioner cannot prevail on Section 23(d).

Accordingly, the judgment is affirmed.

Mr. Justice ROBERTS took no part in the consideration or decision of this case.

Mr. Justice JACKSON.

Since I think this tax was not one on the corporation (See dissent in No. 620, *International Harvester Company v. Wisconsin Department of Taxation*, decided today), I see no basis for the corporation to claim a deduction under § 23(e) of the Revenue Act of 1934. The tax was on the stockholder, and it was paid by the corporation. The Company would be entitled to deductions under § 23(d) if it were not reimbursed. The credit given to the corporation against a declared dividend is in my opinion a "reimbursement" of the corporation for payment of the tax if the Wisconsin Taxing Act is valid. Notwithstanding dissenting views on that subject, I consider myself now bound by the conclusion of the Court. Hence I agree that no right to a deduction exists.

⁶ Hearings before Committee on Finance on H. R. 8245, U. S. Senate, 67th Cong., 1st Sess. 250-251. Compare, e. g., *Elliot National Bank v. Gill*, 218 Fed. 690 (C. C. A.); *National Bank of Commerce in St. Louis v. Allen*, 223 Fed. 472 (C. C. A.); *First National Bank of Jackson, Miss. v. McNeel*, 238 Fed. 559 (C. C. A.).